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THE NATURE OF CAPITALIST CRISIS

# THE COMING STRUGGLE FOR POWER

by the same author

5th impression

"The last three years of depression and crisis have hitherto produced only Sir Arthur Salter's *Recovery* as a considerable addition to thought on the fundamentals of world economic policy. It is just possible that in *The Coming Struggle for Power* Mr. Strachey has made a contribution which will survive when *Recovery* is long forgotten. Several considerations suggest this tribute. First, the book is far the best restatement of the Marxian-Leninist gospel of Communism which has any application to the England of to-day. Secondly, it is the work of a young man of probably unique sophistication. . . . Mr. Strachey has established a range of social, intellectual and political contact that is likely to remain a record. . . . Thirdly, and this is its most attractive quality, the book is lit up throughout by a kind of radiant scientific effrontery. . . . Mr. Strachey faces and analyses many a difficulty from which Sir Arthur Salter, say, would have skated gracefully away."—*Spectator*



# THE NATURE OF CAPITALIST CRISIS

by

**John Strachey**

*Author of The Coming Struggle for Power  
and The Menace of Fascism*

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To  
CELIA AND CHARLES



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## PREFACE

WORKS of economics by non-professional economists are justly suspect. Too frequently their authors have not taken the precaution to acquaint themselves with the main body of existing economic knowledge before setting down their own views. The result has been a great waste of effort. The greater number of amateur economists have either rediscovered truths which were already known, though not to them : or they have fallen into errors which, however plausible, have been exposed in the course of the economic controversies of the last one hundred and fifty years.

And yet both the present state of the science and the present state of the world almost compel every thinking man and woman to examine economics for themselves. For the science is divided into two schools, the capitalist and the Marxist, and these schools are contradictory. And the state of the world is even worse than the state of the science. The condition of the world compels us to attempt the discovery of causes and remedies for our mounting ills. For all around us we see man's newly won power and knowledge being used to destroy our civilization and us with it. Moreover the question of the destruction or development of human civilization is not for our generation an academic or ideal issue. It involves *our* destruction or *our* development. It means life or death to us personally. Peace or war ; plenteous security or cumulative destitution ; these issues involve the lives of every one of us.

But what are we to do ? In order to answer that question a resort to the science of political economy is inevitable. For if we attempt to act without such study, we shall not escape from acting upon the basis of some economic theory : we shall merely rely upon unconsidered, superficial, and so almost certainly fallacious, economic theory. For political economy alone professes to tell us of determinate relationships between our actions, whether collective or individual, and their social consequences. Hence our activities are bound to be profoundly affected by our economic opinions. These are the reasons which to-day compel the study of political economy. These are the reasons which have compelled me to attempt, in this book, to settle some accounts with the science.

The argument of the book compares and contrasts the principal existing explanations of the occurrence of economic crisis : submits reasons for rejecting all except one of these explanations, and finally offers certain remarks upon the significance for practice of this latter explanation. It may be objected that years of cloistered consideration should have preceded such a discussion. The great Professor Taussig is said to have devoted the longer part of his laborious and peaceful life to the study of the effect of tariffs upon international trade. After many years he announced the conclusion that their effect had been exaggerated. Such a model is admirable. But can the contemporary student of political economy hope to emulate it ? He would certainly not be loath to do so, " had he but world enough and time." But he, like the poet, hears a chariot at his back : and it also is winged. The contemporary student hears all around him the clamour of the preparations for those new armed conflicts which, if we remain too long blind to their cause and remedy, will blot out that economy which we study. This must be the apology for all that is rough and incomplete in these pages. The book does not seek to be a work of general economics. It is devoted exclusively to the overmastering problem of our day : namely, the nature of capitalist crisis. More general economic questions are in some places discussed ; but only in so far as the adoption of one theory or another is inevitable to a further attack upon our special problem.

The book will be justified only in so far as it helps the reader to reach settled conclusions as to the nature of capitalist crisis. Millions of men and women are being driven to attempt to find out for themselves the truth about the situation of the world. They realize that not until they are equipped with knowledge can they choose their part. They know that it is only by the light of knowledge that they can see how to strive effectively for security, peace, and civilization. I hope that this book will help them.

My sincerest thanks are due to Mr. Maurice Dobb, and to my wife, who read my manuscript and gave me invaluable suggestions and corrections. It must not be supposed, however, that either of them necessarily endorses arguments or opinions expressed in these pages.



**PART I**  
**CAPITALIST THEORIES OF CRISIS**



## CHAPTER I

### *The Scope of the Enquiry*

DURING the past five years the capitalist world has been going through the successive phases of the most severe economic crisis which it has hitherto encountered.

"The depression has eclipsed all preceding movements of a similar nature both in magnitude and in intensity," writes the Professor of Economics at London University (Professor Robbins).<sup>1</sup> "There is no precedent for such a marked decline," declare the statisticians of the League of Nations. "Statistical series ranging back to 1860 fail to reveal any previous period in which the decline in raw material production or manufactures has been so precipitate or so severe."<sup>2</sup>

Crises are not, indeed, any new experience for capitalism. Great Britain, which was the first country to establish a capitalistic system of production, and the consequential system of the distribution of almost all products by means of exchanges mediated by money, has experienced a dozen of them. And so soon as the capitalist system has taken a firm hold of the economic life of any other people, they also have come to know the effects of these economic earthquakes. Crises have occurred at something like ten-yearly intervals. They have differed enormously, however, in their intensity, in their extension throughout the world, and in their character. Some have been but brief and local earth tremors, while others, and, above all, the crisis which began in 1929, have been seismic disturbances, shaking the economy of the world to its foundations.

In the year 1934 we are all familiar with the disastrous effects of this major disturbance. We have seen a world, which in 1929 fondly believed itself to be entering upon a period of social progress and economic expansion at least equal to the second half of the nineteenth century,<sup>3</sup> flung instead into a period of steep economic decline. We have seen the main bases and underpinnings of world-wide capitalism destroyed. An international

<sup>1</sup> *The Great Depression* (Macmillan, 1934).

<sup>2</sup> *League of Nations World Economic Survey, 1933-3.*

<sup>3</sup> "The outlook for the world to-day is for the greatest era of commercial expansion in history." President Hoover, July 27th, 1928.

monetary standard, a system of international lending, a considerable measure of freedom for the international exchange of commodities, had all been re-established after the world war by extreme efforts and at a painful cost. To-day they are all ruined. We have seen the strongest, richest, and apparently most secure capitalism of all time, the United States of America of the period from 1922 to 1929, especially and particularly cast down: her productivity reduced to an exceedingly low level, her system of exchange paralysed, and for a few days in March 1933 actually interrupted altogether, so that her citizens were unable to obtain any means of payment whatever with which to mediate their transactions.

We have seen even more profound consequences of crisis in the second largest and most advanced capitalist state, in Germany. For, if the crisis never reached in Germany the almost unbelievable point of intensity which it touched in America, it was, and is, more prolonged and all-embracing. The economic significance of the fascist seizure of power in Germany, itself undeniably a consequence of the crisis, is very great. The emergence of a fascist Germany, with its extreme nationalism, the consequential further destruction of the world market, and the intensified growth of armaments and war preparations throughout the world, have in their turn profound economic consequences. For these events go far to forbid all possibility of a return to the relatively peaceful, internationally organized, freely exchanging world of 1929.<sup>1</sup>

The utility of any discussion which can throw light upon the nature of capitalist crisis will not, then, be doubted. But the possibility of comprehending the nature of these extraordinary phenomena will certainly be questioned. For it is true to say that little of significance is universally agreed upon as to the nature, cause, and hence as to the cure, of economic crises. The capitalist world has never been able to discover why its economic

<sup>1</sup> The period from 1922 to 1929 is now widely referred to as a sort of lost golden age, "before the slump." And if our comparison is with the present state of the capitalist world we are justified in such a eulogy. Yet it should be remembered that during those years, at any rate in Britain, and to a large extent in Europe also, we considered that we were living in ruinously hard, desperately insecure conditions—in the midst of an unparalleled depression in fact. For then our standard of reference was the lost golden age of "before the war." These psychological curiosities register declining hopes and standards.

life is periodically thrown into confusion. The very terms in which these events are commonly referred to reveal their mysterious and uncontrollable nature. They are habitually spoken of either as "economic earthquakes" (as here) or as "economic blizzards," or as some such cataclysm of nature. Thus men reveal their impotence to comprehend or prevent them. Capitalist crises are, in truth, to the inhabitants of our highly developed industrial communities, to modern Europeans and Americans, what the tempest and the earthquake are to the savage. Crises destroy our homes, take away our livelihoods, wreck our hopes, and, yes, kill, maim, and starve us by the thousand, just as the forces of nature kill, maim, starve, and destroy the savage. Nor does our attitude to the force of economic crisis differ from his attitude to the blind forces of nature. How could it? When the destroyer is uncomprehended and uncontrolled, when we do not know what to do to guard against his onset, how to combat him when he is upon us, or whether he will return when he has departed, what other attitudes but superstition, propitiation, or resignation are possible?

The savage, it is true, has his experts, his medicine men, who by chant or howl, by sacrifice or incantation, attempt to cajole the destroying force. The capitalist world also has its experts, its economists. The phenomena of crisis lie, however, outside the scope of their science. This fact is not widely realized. Yet there will be no difficulty in citing the explicit admissions of the theoretical experts of capitalism that their science offers no explanation of the existence of crises. They have evolved a science of economics which seems to explain the exact workings of the capitalist system, and (incidentally) justifies those workings in every respect. There is only one difficulty. The system periodically refuses to work. Their science shows conclusively how capitalism adapts itself, smoothly, automatically, perfectly to the ever-changing pull and push of demand and supply; how it maximizes the "net satisfactions" obtainable by the whole population in a way impossible under any other system: how it uses all the factors of production, and uses them all the time, to the best possible advantage for obtaining maximum satisfactions for everybody. Capitalist economic science establishes

the impossibility of any interruptions of production, of any periods of dislocation or of waste—the impossibility, in a word, of crises.

Yet there is, the experts of capitalism agree, an “unexplained residue” of facts which their science does not cover. This “unexplained residue” consists precisely, it turns out, in the fact that crises, heedless of the analysis, occur. Professor Robbins, in his *Nature and Significance of Economic Science*, describes the position with precision.

“The best example of the unexplained residue is provided by those fluctuations of trade which have come to be known as the trade cycle. Pure equilibrium theory, as is well known, does not provide any explanation of the phenomena of booms and slumps. It explains the adjustment of the economic system to external change either on the demand side or on the supply side. It explains fluctuations which are in the nature of orderly adaptations. But it does not explain the existence within the economic system of tendencies conducive to disproportionate development. It does not explain discrepancies between total supply and total demand in the sense in which these terms are used in the celebrated law of markets. Yet unquestionably such discrepancies exist, and any attempt to interpret reality solely in terms of such a theory must necessarily leave a residue of phenomena not capable of being subsumed under its generalizations.”

This passage should suffice to demonstrate the irrelevance to our enquiry of the main *corpus* of capitalist economic theory. This is not to say, however, that individual capitalist economists have not been driven to a consideration of crises. It has become more and more difficult to ignore the existence of those “fluctuations of trade” which to-day convulse the whole world. Economists who blandly refuse to admit of their existence expose themselves to ridicule. Hence various schools of capitalist economists have ventured outside the main generalizations of their science and have attempted to give an explanation of the occurrence of crises. In particular, the school to which Professor Robbins adheres has in recent years devoted attention to the

matter. We shall discuss the crisis analysis of this school, of the other professional capitalist economists who have attacked the question, and of the various types of unorthodox, amateur, but still capitalist, economists who have proffered explanations, in later chapters.<sup>1</sup>

The inability of capitalist economic science as such to consider the existence of crises at all, and the consequent embarrassment of capitalist economists in discussing them, does not, however, make the question any less important for the rest of us. In particular, it is urgently necessary for us to make up our minds as to whether the occurrence of crises is accidental to or inherent in the capitalist system. This is the master question. For upon the answer to it must necessarily depend our attitude to existing society. If we come to the conclusion that catastrophic crises are accidental to capitalism, then we shall certainly work for their gradual elimination by appropriate reforms. For who would be so mad as to recommend the scrapping of the system itself if the catastrophes which it is bringing upon us were remediable? If it were possible so to reform capitalism that it would provide us with an epoch of peaceful, steady, even if gradual, social progress, then none but those who objected to the system upon ethical grounds would work for its abolition. And even they, no doubt, would seek its abolition as the result of a series of cumulative reforms.

<sup>1</sup> It will be well to define at the outset the way in which the term "capitalist economist" is used throughout these pages. For the existence of the category capitalist economics, as opposed to Marxist economics, which we have postulated, will be denied. For example, Professor Robbins remarks, in his preface to Dr. Hayek's *Monetary Theory and the Trade Cycle*, "that there are only two kinds of economics—good economics and bad economics." On reflection, however, I doubt if even Professor Robbins would deny the sheer existence of two traditions of economic thought, the one issuing from the post-Ricardian economists of the last century, and the other from Marx and Engels, however erroneous, confused and pernicious he considered the latter, and however impartial and scientific he considered the former.

We, therefore, who start out on our enquiry with no such pre-suppositions, must recognize the existence of these two distinct traditions of economic thought and must find convenient terms with which to designate particular economists as belonging to one or other of them. Hence we shall call capitalist economists all those economists, whether professional or amateur, orthodox or heterodox, who, belonging to the former school of thought, accept, consciously or unconsciously, the capitalist system of the private ownership of the means of production, their operation for profit, and of the distribution of the products by exchange, as the immutable data of their enquiries.

Indeed, if it were possible so to reform capitalism that it would maintain human civilization even at the level of the last fifty years ; if it were possible to avert the onset of ever worsening crises, with their tremendous train of political and military consequences, then, however bitterly we might detest the system, such a reformed and stabilized capitalism would probably survive indefinitely. If it becomes inescapably apparent, however, that capitalism must in future fail, not merely to provide us with a basis for social progress, but to maintain even our recent level of civilization ; if it becomes apparent that capitalism must certainly plunge us into a new series of ever deepening crises, and that these crises can only bring both international and civil war in their train ; then not only those who have always had good cause to detest capitalism but all reasonable men will find themselves impelled to work for the overthrow of the existing system of society.

Yet unless we can achieve a comprehension of capitalism and its crises we shall never be able to find an answer to this master question. Unless we can discover some law upon the basis of which capitalism works, some law which will enable us to predict the general destiny of the system, we shall remain at the mercy of our own half realized wishes, or of the day-to-day indications of economic recovery or decline. At the moment of writing (autumn 1934), for example, there are in some parts of the capitalist world distinct signs of economic recovery. After five years of unparalleled slump the trade cycle has entered its ascendant phase. As always before, but still more markedly now, the benefits of this recovery are for the vast majority of the population merely some slight relief from destitution. But for the capitalist classes the gains are substantial.<sup>1</sup> The reaction

<sup>1</sup> Profits in England and America are once more rising sharply. In Britain the *Economist* index of business activity had, by the summer of 1934, returned to the boom level of 1929. (It was 107 in 1929 and 107 in August and September 1934.) The *Economist's* figures indicating the rate of profit made by British industry, after dropping for eleven quarters in succession, remained almost steady for two quarters and then increased by no less than 30 per cent in the fourth quarter of 1933, by 5 per cent in the first, by 18.2 per cent in the second, and by 27 per cent in the third quarter of 1934. (It should be noted, however, that these percentage increases are not cumulative. The comparison is in each case with the corresponding quarter of the previous year.) In America, Mr. Roosevelt's Recovery Programme, using violent and novel means, has also secured some increase in the level of production, and has promoted, chiefly by a heavy devaluation of the currency, the reappearance of high profits for many individual firms and corporations.



of many of the theorists of the capitalist world to this fact is unifying. They are demonstrating to even the least acute observers that the varying predictions, the moods of successive optimism and pessimism, the alternating panics and elations, of most capitalist thinkers are but immediate and naïve reflections of the successive phases of the economic cycle. For the indications that the extreme phase of this particular crisis has at length been overcome are being widely hailed as proof that crises themselves have been overcome. Capitalism is now, we are told, well on the road to permanent recovery : all talk of breakdown, of impending wars and revolutions is now happily out of date : an epoch of peace and plenty is opening out before us.

What are we to say of scientists who give way to such " wishful thinking " ? A dozen times now the cycle of boom, crisis, depression, recovery, boom, crisis, has gone through its phases. And as each crisis has passed into depression, and then as symptoms of recovery have appeared to lighten the depression, the shallower prophets of capitalism have told us that at length, but now for ever, all was well. Do they still believe it ? Certainly we cannot.

Another point of view is some times expressed by a more prudent school of capitalist thinkers. It is not denied that crisis and slump will follow the upward phase of this cycle as they have followed every other. But the catastrophic nature which has been here attributed to crises is denied. It is pointed out that capitalist civilization has survived a great many crises before : that the circular path of the trade cycle is well trodden : that no doubt we are treading it again, but that this is no reason for alarmist talk about the destruction of civilization, a new cycle of wars and revolutions, or similar evil prognostications. Such experts certainly show prudence. But they also show a convenient, academic, lack of contact with the real world. For where shall we find a capitalist statesman, an active practising banker, or a great entrepreneur, who will even seek to deny that the collapse of the present recovery and the onset of a new crisis

The index of corporation profits rose from -6.9 per cent in the first quarter of 1933 to +32.2 per cent in the second quarter of 1934. Again the Standard Statistic Company of New York is quoted as showing that the total net profits of 402 representative companies rose from \$47,380,000 to \$335,870,000 between the first half of 1933 and the first half of 1934. (Donald A. Richberg's report on the " New Deal," issued August 27th, 1934.)

would prove the *coup de grâce* for any hopes he may retain of stabilizing his system? There is no scepticism in these decisive quarters as to the inevitability in such circumstances of a new series of wars and revolutions.

A very different criticism of the high importance here attributed to the question of the recurrent crises of capitalism may be made. It may be pointed out that fluctuations in economic activity are not capitalism's essential feature. It may be pointed out that the essential fact of the contemporary situation is that the contradiction between the social relations and the potentialities of production, simultaneously created by capitalism, has driven the system into an ever deepening and now general state of crisis. Hence it is an error to concentrate attention upon the oscillations of the system: the permanent *impasse* down which it has been driven should alone be emphasized. For capitalism has been, ever since 1914, in a state of permanent crisis. This general and permanent crisis, of which the war itself was merely the opening phase, is something, it is urged, distinct from the familiar cyclical crises. And though the cyclical crises are continuing, their importance has now been overshadowed by the general and continuing crisis of the last twenty years.

The fact of a general and continuing state of crisis throughout the existing social and economic system is undeniable. The more responsible capitalist economists themselves recognize the permanent character of the present crisis. "We live," writes Professor Robbins, "not in the fourth, but in the nineteenth year of the world crisis." (*Op. cit.*, p. 1.) *The League of Nations World Economic Survey 1932-3* (quoted above) tells us that from 1860 to 1913 world production increased "with remarkable regularity of trend. . . . If the line of trend from 1860 to 1913 is extended to 1932 the rather startling conclusion is reached that the index of world production, on the hypothesis that nothing had occurred to alter its regular upward trend for the fifty preceding years, would to-day be twice as great as it actually is." In other words, 1914 is the great watershed of world capitalism. Up till that year capitalist production, although interrupted at intervals by cyclical crises, steadily increased. From 1913 onwards the trend is broken, becomes irregular, and, in spite of periodic

booms, the level of production is actually lower at the end of the period than at the beginning. (For a comprehensive exposition of this and much other material of a similar character the reader should consult the three opening economic chapters of R. P. Dutt's *Fascism and Social Revolution*.)

It would be false, however, to separate the study of this general crisis from the study of the cyclical crises. For the cyclical crises are the main economic phenomena in which the general and continuing crisis manifests itself. Moreover, the fact that capitalism declines unevenly, by means of convulsions followed by temporary recoveries, is of the highest practical and political significance. Hence it is necessary and legitimate to discuss this oscillatory process, so long as the background of ever deepening general crisis is sufficiently presented.

#### SUMMARY OF CHAPTER I

Unequalled severity of the crisis which began in 1929. The capitalist world's admitted ignorance of the nature of crises. Inability of capitalist economic science as such to recognize the existence of crises. Urgency of obtaining a comprehension of crises. Our attitude to society necessarily dependent upon whether we think crises accidental to or inherent in capitalism. Impossibility of estimating the permanency of the present recovery, for example, without this knowledge. The relative importance of the cyclical crises, and the now general crisis, of capitalism.

## CHAPTER II

### *Not Enough Money? Major Douglas*

OUR first task is to examine the views of the various schools of thought which have it as common ground that the occurrence of crises is accidental to and not inherent in the capitalist system. For it is only in the event of these theories proving inadequate to the known facts, or in any degree self contradictory, that we shall be compelled to raise the hypothesis of the inevitability of capitalist crises.

In Part I we shall examine the theories of crisis offered by various schools of amateur or heterodox economic thinkers. We shall recount the objections of the professional capitalist economists to these theories. We shall then exhibit and discuss the two theories of crisis offered by the two chief schools of professional capitalist economists which have studied the subject. Finally we shall attempt to summarize such insight into the true nature of the system and its disorders as this survey has given us.

We shall find that the popular, heterodox theories are inadequate to the facts, and that all of them contain errors in reasoning. These insufficiencies and errors will enable the professional capitalist economists to refute them without difficulty. All the same, we shall not find it a waste of time to examine them. These popular and instinctive theories, and the refutations of them, form the best introduction to our subject. Moreover, if the amateur economists cannot provide satisfying answers to our questions, yet, at any rate, they have the merit, as against the latent complacency of many of the orthodox capitalist economists, of insistently calling attention to the extraordinary facts of capitalist crisis.

The most popular and widely supported of the heterodox explanations of the occurrence of crises is some form of what is called the Social Credit theory. It is not to be wondered at that this explanation is popular, for, stated in its most general terms, it is highly plausible. All schools, and there are many, of Social Credit theorists (and this is their great merit) point insistently to the great staring paradox of the modern world. They point to

the fact that we have to-day the technical capacity necessary to the production and distribution of at least a decent sufficiency of commodities for all of us. Yet, in fact, we only produce and distribute sufficient commodities to keep a small proportion of the world's population in decency. This is the famous paradox of starvation in the midst of plenty. It is a paradox which is in danger of becoming hackneyed. Writers and speakers of many schools of thought have harped upon it. They have pointed out its ludicrous and tragic features. They have depicted its most remarkable instances, such as the burning of wheat while millions of human beings lack bread, the carefully organized ploughing in of the American cotton crop while millions of Americans lack shirts, the well arranged destruction of thousands of tons of Brazilian coffee, the recent dumping of millions of oranges into the river Mersey because the Liverpool market was overstocked, while thousands of the people of Liverpool were hungry, the frequent destruction of tons of fish by the same method, and a hundred other such examples.

How can these things be, we all ask ? The Social Credit theorists' answer is a simple one. We know that the reason why millions of us are destitute is not because we cannot produce the things which we need. Therefore we must be destitute because we have not got the money to buy these things. Since we know that it is not production which has failed (for we are busy destroying even what we have produced), it must be consumption. There must be some "flaw" in the present economic system which prevents it distributing enough money to buy the goods which it could, undeniably, produce. The Social Credit theorists proffer an analysis of this alleged "flaw" and a remedy for it based upon that analysis. There are various subdivisions of this school of thought. We shall instance, however, the main contemporary variant, *viz.*, Social Credit theory as expounded by Major Douglas and his followers. For his theory, with this or that unessential modification, forms the basis of the views of all present day "currency cranks," as they are impolitely called.<sup>1</sup>

<sup>1</sup> In dealing with various schools of economic thought it will be convenient to pick out particular individual writers who personify adequately a whole point of view. Thus we shall instance Major Douglas, Mr. Hobson, Professor Irving Fisher,

Major Douglas addresses himself to the great problem which we have just defined. How can it be that while millions of human beings are destitute we are busy actually destroying some of the commodities which we have produced, and that we wilfully refrain from the production of many more?

Now it is undeniable that, whatever may be the ultimate cause, the immediate and proximate reason for this is the fact that most people have not enough money in their pockets to buy these commodities. Major Douglas' conclusion is in essence that the remedy is to give these people some more money. Precisely, however, he would prefer to give the people who want to sell these commodities, the producers and dealers of all kinds, the extra money. Then they would be able to reduce all their prices, and this, of course, if it was done sufficiently, would enable the consumers to buy all the goods which could be produced with even their present stock of money. For when we say that people have not enough money to buy the commodities which we could produce, we mean that they have not enough money to buy them *at their present prices*. If prices were sufficiently reduced, then we could get all the goods we want without having any more money in our pockets.

Why, then, do prices have to be on their present apparently prohibitively high level? It is, is it not, because the prices at which goods are sold must at least cover their costs of production? Anybody who is going to produce and sell commodities cannot sell them at less than they have cost him to produce plus enough profit to himself to make it worth his while to carry on in business. Hence, for Major Douglas, the general predicament in which the world finds itself is, when stated more exactly, that people have not got enough money in their pockets to buy all the commodities which we could produce, at prices sufficiently high to cover their costs of production.

But what are costs of production? They are the amounts which the producers and sellers of commodities have had to

Professor Robbins, Dr. Hayek and others. This method may give the appearance of attaching undue importance to the views of particular individuals. And admittedly the choice of a particular spokesman will in some cases be more or less arbitrary. But I trust that the reader will find that by the end of this section he has not only been given a survey of the theories of some contemporary authorities, but has been led from the periphery towards the centre of the subject.

pay away to other people for working for them at the various jobs connected with producing and selling, plus the amounts paid away by such producers to people who have lent them their capital or their property (interest and rent) for the purposes of production. Thus the producers' costs *are* other people's incomes. How can it be then, asks Major Douglas, that these incomes, which everybody gets by reason of his services in the process of production, or by reason of his lending his property to a producer, are not big enough to buy the products at their cost price? *For these incomes themselves constitute the products' cost prices.* You would have thought that it would be quite certain that costs must equal incomes, and that each must equal prices. And if this were so, all, of course, would be well, for then all the goods produced could be sold at their cost price. How can it be, asks Major Douglas, that this is not so? For it is not so, he believes, or else there would never be crises, slumps, and unemployment.

Major Douglas believes that he has found the reason. He thinks that he has found a gigantic flaw in the whole economic system which makes it impossible for it to distribute enough money by way of costs to give people the money necessary to buy all the commodities produced at their cost price. Here is the passage from his book, *Credit Power and Democracy*, in which he defines what this flaw is. This is the famous "A + B theorem."

"A factory or other productive organisation has, besides its economic function as a producer of goods, a financial aspect—it may be regarded on the one hand as a device for the distribution of purchasing-power to individuals through the media of wages, salaries, and dividends; and on the other hand, as a manufactory of prices—financial values. From this standpoint its payments may be divided into two groups:

Group A—All payments made to individuals (wages, salaries, and dividends);

Group B—All payments made to other organizations (raw materials, bank charges, and other external costs).

Now the rate of flow of purchasing-power to individuals is

represented by A, but since all payments go into prices, the rate of flow of prices cannot be less than  $A+B$ . The product of any factory may be considered as something which the public ought to be able to buy, although in many cases it is an intermediate product of no use to individuals but only to a subsequent manufacturer; but since A will not purchase  $A+B$ , a proportion of the product at least equivalent to B must be distributed by a form of purchasing-power which is not comprised in the descriptions grouped under A."

The reader will see that what Major Douglas has said is that the producers do not, and cannot, distribute to individual consumers all the money which they have to spend in production. If they did, or could, all would be well. But as it is they have to make all sorts of other payments as well, payments which do not go to individual consumers. Such payments consist of the price of the raw material which they have to buy, bank charges, and "other external costs," as Douglas puts it. And producers have to charge a price for their finished goods which will cover *both* of these kinds of payments. Yet only one of these kinds of payments has gone to make up individual consumers' incomes. And individual consumers' incomes form, Major Douglas tacitly assumes, the only money that there is with which to buy commodities. Hence, by simple arithmetic the unfortunate consumers—that is, all of us—can never have enough money to buy all the commodities produced at prices sufficient to cover all the payments out which had to be made in the course of their production—to cover, in other words, their costs of production.

What have the professional economists got to say about that? I am afraid that they have got a good deal to say. It is possible to refute Major Douglas'  $A+B$  theorem in many different ways. It will be worth while to look into some of them, for the points raised will be useful to us in later stages of our argument.

Let us admit at once that Major Douglas proves conclusively that we, the individual consumers, do not get enough money to buy *all* the commodities which are produced at prices which will cover their costs. Have we not thus admitted the whole of Major Douglas' case? But let us look for a moment at all these commodities. What do they consist in? We are apt to think of all



commodities as consisting in things we want, like bread, or coats, or shirts, or jumpers, or furniture, or motor-cars, or books—of what the economists call “consumers’ goods.” But are all the commodities produced and offered for sale at any given moment of this kind? No, they are not. All sorts of things like lathes, steam hammers, steel billets, locomotives, raw cotton, unbleached wool, unground corn, raw rubber, asbestos fibre, iron ore—in a word, what the economists call “producers’ goods”—are also being offered for sale.

Hence the question we have to ask is, would it be a good thing if we individual consumers had enough money distributed to us to buy *all* the commodities which are produced—all of the producers’ goods as well as all the consumers’ goods? This raises the question of what we should do with the producers’ goods when we had bought them. We suddenly get a vision of the housewife returning from her morning’s shopping with her basket full, not only of her usual groceries, but also of a lathe, some raw cotton, some wheat, some pig-iron, and a locomotive. Now it is quite true, as Major Douglas says, that all the housewives, who may stand for all the consumers of the country, do not have enough money distributed to them to buy all these commodities—all the producers’ goods as well as all the consumers’ goods. But in proving this has Major Douglas succeeded in showing that anything is wrong with the present economic system? We see already that he has not.

The truth of the matter is that there is no need for us individual consumers to have enough money distributed to us to buy all the goods that are produced. All we need is enough money to buy all the *consumers’* goods that are produced. (It remains to be seen whether we get enough to do that.) We see what a tremendous difference is made by this distinction between producers’ and consumers’ goods when we realize that it is usually calculated that in highly industrialized countries like Britain and America no less than nine-tenths<sup>1</sup> of all the goods produced and offered for sale at a given moment consist of producers’ goods. Nine-tenths of all the goods on the market

<sup>1</sup> Nine-tenths in Britain, ten-elevenths in America, according to Mr. Hugh Gateskill’s and Mr. E. F. M. Durbin’s papers in *What Everybody Wants to Know About Money*.

are of a kind, that is to say, which would be quite useless to us even if we had the money to buy them. Hence we only need enough money to buy one-tenth of all the goods which are produced, for these alone are any "good" to us.

Again, consider what would happen to the productive system if we did buy all these, to us, useless producers' goods. Not only should we soon have our houses completely filled with lathes, locomotives, raw cotton, and unground wheat, but the production of next month's supply of consumers' goods would become quite impossible. We should have stripped the productive system of both its fixed and its working capital. We should have made all future production quite impossible.

Now look again at Major Douglas' statement of the A+B theorem. What must be our surprise to notice that this crushing objection to it is actually alluded to in one of the sentences of the theorem? "The product of any factory," we are told, "may be considered as something which the public ought to be able to buy, although in many cases it is an intermediate product of no use to individuals but only to a subsequent manufacturer." But then why may it "be considered as something which the public ought to be able to buy"? Why ought the public to be given enough money to buy "an intermediate product of no use to individuals"?

Finally, Major Douglas, we recall, finds that many of the payments out of the producers, which have to go into cost prices, are made, not to individual consumers, but to what he calls "other organizations." These are his B payments, and they consist of payments for "raw materials, bank charges, and other external costs." These payments go, he says, to "organizations," to Joint Stock Companies, Corporations, Public Departments, Municipalities, and the like. Yes, they do, and these "other organizations" are, in fact, just the bodies which do need the producers' goods which we have described above. The cotton-spinning companies buy the raw cotton, the railway companies buy the locomotives, the iron and steel works buy the iron ore, and so on and so on. So what is wrong with an economic system which, as Major Douglas himself shows, distributes the money necessary to buy these producers' goods, not to individuals, to whom they would be useless, but to

"organizations," which are, in fact, just the people who need them? It will be seen that Major Douglas' basic fallacy is to confound in various ways the distinction between producers' and consumers' goods.<sup>1</sup>

It will be seen from our distinction between the two great classes of commodities, producers' goods and consumers' goods, that there must be two great departments of the productive system to correspond to these two main kinds of products.<sup>2</sup> There must be one class of capitalists who specialise in making producers' goods, and another class who specialise in making consumers' goods. And so there are. Now Major Douglas concentrates his attention on the second of these departments—the one making consumers' goods—and he notices that the costs of the firms which make up this department do not consist by any means entirely of payments to individual consumers. Let us take a tailor who makes and sells suits. Some of his costs consist in wages to his cutter and rent to his landlord, and other such payments to individual consumers. But another portion consists in payments for his raw material—his cloth, buttons, and so on. As a matter of fact, much the greater part of the costs of the producers of consumers' goods consist in this latter kind of payments, *viz.*, payments which do not go to individual consumers. Only a small part of their costs goes to individual consumers and is, therefore, available as income to buy the final product. And yet the goods which these firms produce have got to be priced high enough to cover all these payments out by way of costs. How is it possible then, asks Major Douglas, that they can be sold? But Major Douglas forgets to look at the other department of industry, the department making

<sup>1</sup> Naturally, Major Douglas has not been able to remain unaware of this distinction and there are many passages, especially in his later works, in which it is recognized. But what is not, unfortunately, recognized is the fatal effect of this distinction on the A + B theorem.

<sup>2</sup> This is one of Marx's favourite ways of depicting the productive system. See Vol. II. of *Capital*, p. 457, and throughout the rest of the argument of this volume. See also, and more particularly, Marx's refutation of J. B. Say's "Douglasism" in Chapter xlix of Vol. III. Say, whose unfortunate person provides Marx with a sort of whipping boy throughout the three volumes of *Capital*, not content with having collected most of the economic errors of his own day, seems to have anticipated the fallacies of our century. As a matter of fact, however, the basic illusion upon which Douglasism is founded kept cropping up all through the nineteenth century. For a refutation of it in the form adopted by Rodbertus, see Engels' elegant preface to the English edition of *The Poverty of Philosophy*.

*unconsumable* goods, or producers' goods, which are no use at all to individual consumers. This department of industry, however, is paying out money to individual consumers all the time. The workers in the iron and steel industry are drawing wages, the landlords of the ground on which power stations are built are drawing rent, the workers making the tools and generators for these stations are drawing wages; the workers in the wool textile industry, who wove the cloth for the tailor, are getting wages. But none of these workers are producing anything which they themselves want to buy. They are producing no finished consumers' goods.

Now we begin to see the real position. One department of industry, the consumers' goods department, produces all the goods which the individual consumer buys, but it only distributes a small part of the money necessary to buy these goods. The other department of industry, the producers' goods department, produces no consumers' goods, but it distributes to individuals all the rest of the money necessary to buy the available consumers' goods.<sup>1</sup> Think what would happen if the consumers' goods department distributed all the money necessary to buy the available consumers' goods. The workers and capitalists in this department would snaffle the community's entire output of consumers' goods. There would be no consumers' goods at all left over for the unfortunate workers, capitalists, and landlords in the producers' goods department. They would all have to go without any consumers' goods and attempt to subsist upon a diet of pig-iron and raw wool.<sup>2</sup>

We can now see how appallingly much too much Major

<sup>1</sup> Here, however, lies concealed an important consideration. If it is true that the greater part of the money necessary to the purchase of the community's output of consumers' goods is only distributed via the producers' goods department, then it is clear that anything which interrupts activity in that department will at once react upon the demand for consumers' goods. It looks as if most of us were dependent under capitalism upon money paid to us for working in the producers' goods department. Hence any interruption in the production of producers' goods will create a situation in which not enough money is distributed to individual consumers to buy the available consumers' goods; will create, in a word, the very situation which Major Douglas describes. At a later stage in the argument we shall be able to elucidate this point. We can, if we like, regard this as the element of truth lying at the bottom of Major Douglas' thesis.

<sup>2</sup> Naturally the departments of industry are not so clear-cut as we have made them sound in this diagrammatic presentation. But all the complications which realism would introduce would not, as the reader will be able to see, affect the argument.

Douglas' theorem seems to prove. Major Douglas himself does not quite seem to realize it, but, as we have shown, people in fact only get one-tenth of the money necessary to buy all the goods produced and offered for sale at any given moment. (At prices that will cover costs, it is always understood, of course.) And so if, as Major Douglas thinks, it is necessary, in order to keep industry going, to give people enough money to buy all the goods produced, the present position must be desperate indeed. If Major Douglas is right, only one-tenth of the goods now produced can be sold, or, alternatively, they can all be sold at prices equal to one-tenth of the cost of their production. In either case, surely, utter and total bankruptcy for every single firm must result within twenty-four hours? And yet even the most embittered critics of the capitalist system do not claim that every capitalist firm goes bankrupt once every twenty-four hours. From mere observation something must be wrong with the  $A+B$  theorem.

Now let us stop thinking of the productive system as a whole. Let us consider, instead, the production of one particular consumers' commodity—a suit of clothes. It is clear that several organizations, usually Joint Stock Companies, are nowadays needed for the production of a suit of clothes. There are, that is to say, several stages of production starting from the basic raw material, and each stage is, usually, undertaken by a separate firm. Let us for simplicity's sake think of the production of a suit in four stages (actually there are more). It is a sort of industrial "House That Jack Built." There is the farmer who rears the sheep, to grow the wool, to weave the cloth, to make the suit that Jack wore.<sup>1</sup>

More exactly, there is Stage I, the production of the wool by the farmer; Stage II, the dyeing, cleaning and preparing of this

<sup>1</sup> I take the image from Mr. E. F. M. Durbin's contribution to *What Everybody Wants to know About Money*. For a copious refutation of Douglasism and of three other varieties of Social Credit theory, see also Mr. Hugh Gateskill's paper in the same book. Mr. Durbin has also given the same argument as an appendix to his *Purchasing Power and the Trade Depression*. These two capitalist economists rely almost entirely on the fourth of our refutations—the one which deals, not with the aggregates of social production, but with the production of an individual commodity. We shall see in Part II that this choice of approach was to be expected.

wool by a firm of dyers ; Stage III, the weaving of this wool into cloth by a weaving firm ; Stage IV, the cutting of the cloth into a suit by a firm of tailors. (Once again the division into four stages instead of six or seven stages is quite arbitrary and may flout all sorts of technicalities. But the argument is just the same so long as it is admitted that there is more than one stage.)

Let us, for arithmetical simplicity and without regard to the real proportions, say that it cost the farmer £1 to grow the wool. And when we say that it " cost " the farmer £1 to grow the wool we must count not only his direct payments out by way of wages to his shepherd, rent to his landlord, and the like. We must also count a sufficient sum to keep in repair his fixed capital, to keep up his fences, to clear the drains of his pastures, and to rethatch his barns. For the farmer must be able to lay aside so much a year for the " amortization," as the accountants would say, of his capital. And on top of this we must count a certain minimum amount of profit on which our farmer and his family must live. Nor are these two latter items of costs any less necessary in the long run than wages and rent. For unless they are forthcoming the farmer will not in the end be able to go on growing wool. (And this applies equally to the other stages of production.)

Since, then, it cost (in the above inclusive sense of the word) the farmer £1 to grow the wool, he must sell it to the dyer for £1. Let us say that it costs the dyer another £1 to dye and clean the wool. Therefore he must sell it to the weaver for £2. Let us say that it costs the weaver another £1 to weave it into cloth. Therefore he must sell it to the tailor for £3. And let us say that it costs the tailor another £1 to make the suit. Then the tailor must sell it to Jack, the ultimate individual consumer, for £4. Therefore Jack must have £4, no less, in his pocket if he is going to buy the suit at a price which will cover its cost of production.

But Major Douglas thinks that Jack ought to have enough money in his pocket to buy not only the suit, but the wool, the cleaned and dyed wool, and the cloth as well. Now if you add up the cost prices of the wool, the dyed and cleaned wool, the cloth, and the suit, you will see that they come to £1+£2+£3+

£4=£10. So Major Douglas thinks that Jack must have £10 in his pocket in order to keep the wheels of industry turning. Jack, however, does not want the raw wool, the dyed wool, or the cloth. And, if he bought them, he would become Jack cormorant, Jack ogre—a Jack who stripped off all the capital from the productive system. He would make it impossible to get another suit when he wanted one next year.

Finally, let us see whence Jack got the £4 which it was necessary for him to have in order to be able to buy the suit. Who is Jack, the ultimate individual consumer? Jack the consumer, who goes into the tailor's shop and buys the suit, is also in his working hours Jack the producer. The farmer and his shepherd who reared and sheared the sheep are Jack. They are, that is to say, consumers who buy suits. The partners in the firm of dyers and their workers are consumers, and so are the wool textile workers, and so are the tailor and his cutter. Now what have these people been paid in the course of the production of the suit? The farmer and the shepherd, we know got £1, which was paid them by the firm of dyers. The workers and capitalists of this firm of dyers also got £1, for they were paid £2, we saw, by the weaving firm. And they had only to pass on £1 to the farmer. In the same way, the capitalists and workers of the weaving firm got £1 for themselves as they were paid £3 by the tailor and only had to pass on £2 to the dyers. And the tailor and his cutter also got £1, for they were paid £4 by Jack, the ultimate consumer, and only had to pass on £3. Now, if you add up these sums paid to the ultimate consumers during the processes of production, you get :

Farmer, etc..	.	.	.	.	.	£1
Dyers, etc.	.	.	.	.	.	£1
Weavers, etc.	.	.	.	.	.	£1
Tailor, etc.	.	.	.	.	.	£1
						—
						£4 in all.
						—

Now the farmer and his shepherd, the dyer and his "hands," the weaver and his "hands," and the tailor and his cutter, are the individual consumers. And there was distributed to them just

*precisely the £4 necessary to buy the final finished product at a price which would cover its cost of production.*<sup>1</sup>

Another way of stating Major Douglas' error is to say that he has not allowed for the fact that in existing society buying and selling have penetrated deeply into the productive process itself. The larger part of all the buying and selling that goes on consists in transactions between different kinds of producers. For example, the steel industry buys coal from the mining industry, the engineering industry buys steel from the steel industry, and the mining industry in turn buys machinery from the engineering industry. There is a vast and necessary process of buying and selling by which industries take in each other's washing. Hence a large part of our output of saleable goods and services does not, and cannot, reach the individual consumer. Similarly, a large part of the community's stock of money must be used for effecting these inter-industrial transactions.

The fact that Social Credit theory is based on a failure to allow for this fact is vividly illustrated by an account which we have recently been given of how Major Douglas discovered his basic theorem. This account is to be found in a presumably authoritative description printed on the cover of *The Douglas Manual*.

<sup>1</sup> Douglasites when pressed are apt to fall back on the argument that if most B payments do go to consumers at an earlier stage of production, yet surely this is not true of that part of costs which is represented by the necessary amortization of capital. But what possible reason is there to suppose that the money which has to be used for capital renewals does not also become, and just as quickly as do other costs, the individual incomes of the producers of capital goods? We showed that a necessary part of the cost of producing the wool to make Jack's suit consisted of money laid aside by the farmer for renewing or repairing his agricultural plant and machinery, buying new carts, rethatching his barns, and the like. But this money is the income of the thatchers, the wheelwrights, and the other producers of capital goods, and these people spend their incomes on consumable goods. There is no more truth in this refuge of Douglasism than in its main original proposition that no B payments go to individuals.

As a final resort supporters of Major Douglas are apt to assert that in any case the money which goes to the thatchers and repairers of barns (the money spent on the amortization of capital) does not become individual income so quickly as does the money spent on direct wage costs, for example. Not only is this contention erroneous; the reverse is the case. The money spent on the repair, renewal, or creation of fixed capital has to be spent before, not after, that fixed capital can be used for producing consumers' goods. Hence this money often becomes the income of individuals before the consumers' goods, which the individuals who receive it wish to spend it on, have been produced. This consideration has led one school of professional capitalist economists to allege, as we shall see, that not only enough, but too much, money to buy all the consumers' goods produced at prices which will cover their costs of production, is often distributed.



This useful work contains a recension of the key passage from all Major Douglas' works, compiled "with the author's full approval" by Mr. Philip Mairé. Major Douglas, it seems, came on his theorem as follows :

"While reorganizing the working of the Farnborough Air Factory during the war and devising a new method of keeping accounts, Major Douglas' curiosity was aroused by his observation that the total costs incurred in each week were greater than the sums paid out for wages, salaries and dividends in that week. If this was true, as presumably it must be, for all productive businesses, it would surely invalidate the theory upon which our whole financial system was supposed to work—namely, that all costs were distributed as purchasing power. Major Douglas proceeded to collect information from over a hundred large businesses in Great Britain and found that in every case the total costs incurred in every week were greater than the sums paid out for wages, salaries and dividends—except in businesses heading for bankruptcy."

We are now in a position to see that if Major Douglas had enquired of every single business in the country he would have got the same results. For *every* business distributes less purchasing power to individuals by way of "wages, salaries and dividends" than will buy the products which it puts on the market. For all these businesses are buying from and selling to each other. Hence much of the country's stock of money is not distributed to individuals. And this is as it should be, for much of the product of industry is not, and cannot be, distributed to individuals either.

Thus all ends happily. The professional capitalist economists have little difficulty in disposing of Major Douglas and his friends. The capitalist system, it is demonstrated, has been much maligned. There is no "flaw" in it. All is for the best in the best possible of worlds.

We may retain our own opinions as to that. But it is true that the theoretical foundation on which Social Credit theory is raised will not stand examination. We have discussed Social Credit in this chapter from a strictly and narrowly economic standpoint, however. And this is not how its supporters usually

regard it. Indeed, the impression which the reader of, for example, *The Douglas Manual* will obtain is that the  $A+B$  theorem plays a quite subordinate part in the *corpus* of the theory. In fact, that theorem is fundamental and Major Douglas' theoretical structure collapses, since  $A+B$  cannot be substantiated.

Still, Social Credit theory does not form a closely knit whole. Major Douglas is essentially an empiricist. And in some respects he is an acute observer. Thus the first thing which will strike the reader of *The Douglas Manual* is its sustained protest against the ever growing tendency to the *centralization of capital*, and the growth of monopolistic forms within capitalism. (See *Social Credit*, pp. 153-4, and *The Monopoly of Credit*, pp. 83-4, for instance.) "The characteristic of orthodox Finance is the centralization or monopoly of Credit," writes Major Douglas (*Warning Democracy*, p. 73). It would be more accurate to say that a characteristic of contemporary capitalism is the centralization or monopoly of the control and ownership of the means of production. But unquestionably Major Douglas is here pointing to a real and extremely important phenomenon. He is excellent, too, on the control which this monopoly (and it is, predominantly to-day, a monopoly of finance capital) exercises on the Government machine, through the Liberal, Labour and Conservative Parties alike: and he sees clearly the drive of the present system to war.

Major Douglas is essentially the champion of the small- and medium-scale independent producer who is to-day being crushed out of existence by the trusts and trustified banks. This, indeed, is the essential social characteristic of the Social Credit movement. This is what gives it its measure of vitality. Social Credit theory is not just an economic fallacy, as the professional capitalist economists would have us suppose. It is also a well-founded, though necessarily confused, cry of protest, raised by the remaining independent producers against the ever growing domination of the great monopolistic capitalist groups. And it is true that these monopolists work largely (although not exclusively) through their hold over liquid finance capital (or "credit") mobilized in the banks.<sup>1</sup>

<sup>1</sup> The quintessentially *petit bourgeois* character of Social Credit is amusingly revealed by certain of Major Douglas' turns of phrase. Thus in *These Present*

Moreover, as we hinted in the footnote on p. 30, it is possible to detect in the A+B theorem a reaching out after the central contradiction of capitalism, namely, the conflict between the accumulation of capital and the distribution of consumers' goods. More especially in some passages in which the original proposition contained in A+B appears to be modified (see especially *The Monopoly of Credit*, pp. 36-7) Major Douglas catches a glimpse of the idea that the object of capitalist production is the accumulation of capital, and that the distribution of purchasing power to individual consumers is dependent upon the perpetual enlargement of that process. Unfortunately, however, he more often suggests that the object of capitalist production is the provision of consumers' goods. We are not yet in a position, however, to discuss this question.

When all is said and done as to the genuine motivation of the Social Credit movement, we may still find it hard to credit the undoubted fact that all over the world there are many thousands of people who pin a passionate faith upon the A+B theorem, and the remedial policy which is based upon it. But such incredulity is naïve. The fallacy upon which Major Douglas' theorem is based is a simple one. In essence, it is a failure to distinguish adequately between producers' and consumers' goods. There is no truth in Major Douglas' views, if we mean by truth correspondence with reality. But there is a profound truth in his views if we mean by truth correspondence to the most heartfelt wishes of some sections of the community. As what is called "wishful thinking," the theories of Social Credit are of unrivalled perfection. The promises which they hold out to a suffering world are attractive in the extreme. They tell us that by a reasonably simple readjustment in the technique and policy of banking, by the issuance, either to producers or to consumers, of a great deal more money (and who quarrels with

*Discontents and the Labour Party* (p. 7) he writes, truly enough, that "the intellectual is apt to fail in interpreting the great mass of humanity engaged in a deadly battle with the weekly household bills." Now "the great mass of humanity," the 33 million non-income tax payers of Great Britain, for example (see p. 144) have never handled "a weekly household bill" in their lives. They have to pay cash—or to run into uncontrolled debt—with the local tradesmen. The struggle with "the weekly household bills" is the struggle of the lower middle class. It is this class, its problems and its sufferings (and to-day this class is beginning to suffer), which fill the unconscious background of Major Douglas' mind, even when he genuinely thinks he is talking about the workers.

getting more money ?), not only can the present economic tragedy be abolished, but an era of unparalleled plenty, combined with extremely short hours of work, be immediately introduced.

Moreover, all this can be done without any painful or costly social upheaval. The capitalists can all be allowed to continue in full legal possession of their capital. They can go on drawing profits—far higher and more secure profits than they are drawing at present—and yet no worker need lack for all the commodities which any reasonable man could desire. When we realize that these promises are backed by reasoning which has a certain momentary plausibility we cease to wonder at its widespread appeal.

Moreover, the undeniable fact remains that Major Douglas and the other theorists of the Social Credit movement do point persistently to the master paradox and master tragedy of our age. Their analysis of that paradox and their proposed solution of it are alike fallacious. They fall an easy prey to the refutations of the professional capitalist economists. But, though these economists can refute the Social Credit analysis, they cannot themselves offer any adequate alternative. Hence we can have little patience with any complacency on the part of the capitalist economists when they have destroyed the Douglas theory. If Major Douglas and his friends are unable to explain the ever recurrent and ever growing crises of capitalism, so are they. He is wrong ; they are merely impotent.

#### SUMMARY OF CHAPTER II

Part I devoted to a consideration of the views of those who think that crises are accidental to, not inherent in, capitalism. The views of the amateur economists first considered. The Social Credit theory : Major Douglas selected as spokesman. The A+B theorem explained. The refutation of Douglasism. His failure to distinguish adequately between producers' and consumers' goods seem to be his basic fallacy. His failure to provide consumers' goods for the workers and capitalists

of the producers' goods department of industry. He proves too much. The industrial house that Jack built. How Major Douglas made his discovery. The social motivation of Social Credit. Douglasism as wishful thinking. Sterility of professorial critics of Douglas.

### CHAPTER III

#### *Not Enough Money ?*

*Mr. J. A. Hobson. and Professor Irving Fisher*

WE have reviewed the Social Credit arraignment of the existing economic system. Major Douglas and his friends charge that it does not distribute enough money to individuals, by way of costs, to enable them to buy all the commodities which they themselves have produced. We found that this arraignment is true but irrelevant.

Capitalism does not distribute enough money to enable individual consumers to purchase all the produced commodities at a price which will cover their costs of production. Indeed, it only distributes to individuals a small part of the sum which would be necessary for this purpose. But, then, neither do the individual consumers wish to purchase all these commodities. On the one hand, they would have no use for some nine-tenths of them, and, upon the other, their purchase by them for (attempted) individual consumption would strip the productive system of all its working and of much of its fixed capital, and so render all future production impossible. For nine-tenths of the commodities at present produced and offered for sale are what are called *producers' goods*—things like raw steel, unbleached wool, or machine tools.

Finally, we found that the present system apparently does distribute to individuals just precisely enough money to enable them to buy all the *consumers' goods*—all the bread, the boots, the seats in railway carriages, and the like, which have been produced. Our personified consumer, Jack, received just £4 for his various activities in producing the suit of clothes. £4 was precisely the price at which the suit had to be sold in order to cover its cost of production (which we saw included necessary profits and amortization). Jack spends his £4, buys the suit, and all is perfectly well.

The social credit arraignment breaks down. And yet, let it be said once again, the problem remains. The notorious and inescapable fact is that periodically Jack the consumer does not and cannot buy the suit. Somehow or other, evidently not for the

reason Major Douglas supposes, but for some other reason, Jack does not, whenever there is a crisis, receive sufficient money to buy the consumers' goods which he produces. Moreover it is clear that Jack never nowadays receives enough money to buy all the consumers' goods which he *could* produce.

At the time of writing (summer 1934), for example, the British consumers can only buy something like two-thirds of the consumers' commodities which could be immediately produced. Accordingly some third of all the Jacks in their capacities of consumers are destitute, and in their capacities as producers are unemployed. We are back at the hard, undeniable, monstrous paradox of the co-existence of enforced want and enforced idleness.

Let us seek another interpreter who may unriddle for us this master riddle of our age : another champion against the professional capitalist economists. We will select another thinker who holds views of the same general type as Major Douglas, although of a much more moderate kind. Mr. J. A. Hobson, the most distinguished of the amateur, heterodox economists of capitalism is perfectly aware of the distinction between producers' and consumers' goods. He would not, I think, challenge the refutation of Social Credit which we have just exhibited. He does, however, consider that crises are due to a deficiency in the purchasing power which the system distributes to individual consumers, and he does believe that this flaw in the system can be remedied by an appropriate issue of more money. He belongs, in a word, to that very wide category of thinkers who are often called "under-consumptionists," because they believe that our troubles are caused by a failure in the consumptive power of society. We shall find that this category cuts across our previous one of amateurs and professionals. For, while all amateur capitalist economists are under-consumptionists, so to-day are many of the professionals.

Mr. J. A. Hobson takes up the story just where we left off. We had demonstrated that Jack the consumer gets just enough money to buy, at prices which cover their costs of production, the consumers' goods which he has produced. The suit cost £4 to produce : Jack was paid £4. If he spends his money he can buy the suit. *But does he spend his money ? Does he spend all of*

*it?* This is the pertinent question asked by Mr. Hobson. No, he does not, Mr. Hobson replies. He *saves* some of it—say 5s. of the £4—and all is lost!

We see at once the nature of Mr. Hobson's diagnosis of the trouble. Jack was only paid £4, not a penny more. The suit cost £4 to produce, not a penny less. But now, since Jack has turned thrifty and put 5s. in the Savings Bank, he has only £3 15s. left to spend. *He cannot buy the suit at a price which will cover its cost of production.* Nor need we doubt the relevance of this diagnosis to the real situation. On the "professionals'" own showing, the body of consumers only get precisely enough money to buy all the consumers' goods produced, at a price which will cover their costs of production. Nor can we doubt that Mr. Hobson is right when he submits that the consumers do not in fact spend all the money that they get. They certainly do save some of their incomes—they even glory in doing so! This act of saving, which we begin to suspect as the arch-villain of the piece, is openly and notoriously practised by all the richer consumers at any rate. But what, then, is to happen to the consumers' goods? How can they be sold at prices which will cover costs? In order that the system may work, it is clear that the individual consumers' total incomes must equal the total prices of all the consumers' commodities produced. (Or, as the economists write it in their shorthand, costs=incomes=prices.) But now we see that one, and apparently one alone, of these items, namely incomes, has something, namely savings, subtracted from it. Therefore incomes cannot equal costs or prices. What can happen? Obviously Mr. Hobson alleges, the consumers' goods cannot all be sold at prices which will cover their costs. Either some of them must remain unsold or, as will naturally happen in practice, competition will drive down the prices of all of them. But we know that their original prices were only equal to their costs. Hence their new, lower prices must be below costs.<sup>1</sup> The effect of saving, argue Mr. Hobson and his school, must be steadily and continuously to push down the prices of consumers' goods,

<sup>1</sup> I take this demonstration of the apparent opening for Mr. Hobson's argument provided by the orthodox refutation of Social Credit from Mr. E. F. M. Durbin's *Purchasing Power and the Trade Depression*. We are in these chapters traversing the same road from Left to Right, from the extreme inflationists to the extreme deflationists, as that followed by Mr. Durbin. Our destination, however, is different.



and thus to force them below their costs of production. But producers cannot long go on selling at below costs. They will go bankrupt if they do. And this is just what does happen. As soon as the effect of saving has operated for a sufficiently long time prices are forced below costs and producers begin to go bankrupt: in a word, there is a crisis. What further need have we to look for the cause of capitalist crises?

Here, in briefest outline, is Mr. Hobson's diagnosis. If he is right, the remedy is obvious. There is no need "to overthrow the capitalist system," or do anything desperate or drastic of that sort. All that we need do is to issue enough new money to balance the amount that consumers save. The deficiency in incomes caused by saving must be made good by a steady but gentle expansion of credit. There will be nothing inflationary about this, we are told: it will not raise the price-level. All it will do is to prevent the price-level from dropping—from dropping below costs, and so causing crises. It will achieve a permanently stable price level—with all that such an achievement would mean by way of economic stability and social justice. Moreover, matters can so be arranged that the expansion of credit can be very moderate. For it need only be equal to savings. Hence, the more savings are diminished the less need there will be for new credits. How, then, can saving, since saving is at the root of the trouble, be abated? The method is clear. Mr. Hobson proposes to redistribute income by way of taxation of the rich and the extension of social services to the poor, so as to secure greater equality. For this will certainly minimize savings. A man on £8 a week will usually spend all his income, while a man on £300 a week will almost certainly save some of his. We see at once that Mr. Hobson's view forms an economic justification for the Liberal and Labour programme of progressive Social Reform. The debt of the British Labour Party, the Independent Labour Party, in its "Living Wage" period, and of all thinkers of the non-revolutionary Left, to Mr. Hobson is not usually realized. In fact Mr. Hobson is the main source of the ideas of all this school of thought in Britain, and to a smaller extent in America. (See Mrs. Barbara Wootton's book *Plan or No Plan?* for an elucidation of this point.)

Well, what have the "professionals" to say about all this? Mr. Hobson's case seems very strong. The "professionals" themselves have shown that total prices cannot possibly be greater than total incomes. Hence, if you take savings from incomes, prices too must be forced down. Here, surely, is an arithmetical truth. How can it be denied? How can it be denied that Mr. Hobson is right when he says that the existence of savings, unless compensated for, must mean a steady and continuous fall in the price-level of consumers' goods? The answer is that this proposition is not denied.<sup>1</sup> But what the professionals do deny are the consequences which Mr. Hobson deduces from it. They deny his key corollary that a drop in prices must mean that prices are driven below costs. How so? Have they not themselves shown that prices were originally equal to costs? If prices now drop, because of a deficiency in the purchasing power of incomes caused by savings, must they not, by hypothesis, be driven below costs? No, they must not, say the professionals: and for the simple reason that costs will be dropping too, and dropping just as rapidly as prices. For the same factor, savings, which is depressing prices, will be also, and equally, depressing costs.

Mr. Hobson, they say, has forgotten the other side of the operation of saving. For what happens to the money which has been saved? It isn't just thrown down the drain: it isn't just hoarded in a stocking.<sup>2</sup> In modern conditions practically all of it is invested. And what does "invested" mean? It means "spent upon producers' goods."

The process of saving is, then, a process by which the individual consumer lends part of his income to organisations which purchase producers' goods. And it is this positive, investing, side of the process of saving which, say the professionals, effects that all-important reduction in costs which prevents prices being driven below costs.

For investing means ordering, and consequently producing,

<sup>1</sup> See Dr. Hayek's conclusive criticism of Wicksell, who supposed that it was possible for the banking authorities to refuse to expand credit and yet prevent savings from depressing the price level. (*Prices and Production*, pp 23-4.)

<sup>2</sup> It is worth noticing, therefore, that if and when savings are hoarded, the effects foretold by Mr. Hobson will follow. This is an important point of Mr. J. M. Keynes' crisis analysis.

new producers' goods. But why do people order new producers' goods ? They do so because they believe that these new producers' goods will enable them to produce new consumers' goods *more cheaply* than they are being produced at present, and so make a nice profit for themselves. For they will be able to sell their new consumers' goods at prices which will cover the costs of production of the other consumers' goods which are still being produced in the old, more expensive, way. But their new methods of production, operated by means of their new producers' goods (new automatic lathes, or looms, newly introduced raw materials, or what not), will enable them to work with costs lower than the average. The difference between their costs and average costs will be all profit for them.

Undoubtedly this is the motive which induces people to invest, *viz.*, the expectation of profit to be derived from producing commodities by improved methods, and so at costs below the average. Moreover, we are enabled to estimate how much below average existing costs the improved methods continually being developed will enable production to be carried on. For the same people do not usually do the saving and the investing. The investors are active "*entrepreneurs*"—employers of labour.<sup>1</sup> The savers are the general public. So the investors have to borrow the money from the savers. And a *rate of interest* is established : a rate, that is to say, which the active, enterprising *investors* will give to the savers for the use of their money. And what can this rate of interest be, say the professional capitalist economists, but the anticipated difference between the costs of producing by the old methods and the new, minus a rate of profit for the investors sufficient to cover their risks ? Therefore the very existence of such a thing as a rate of interest proves that the creation of new producers' goods will lower the costs of production of consumers' goods by a percentage greater than the prevailing rate of interest. For what except this reduction in costs of production enables the enterprising investors to pay the savers a percentage on their money ?

<sup>1</sup> The reader will notice that we are using the word "invest" in a technical sense, differing from its everyday use. Usually we talk about the ordinary individual saver "investing" when he buys the stock of some new issue. But actually, of course, what he does is to lend his money to the promoters of some new enterprise, who then do the actual "investing," *viz.* the actual ordering of the new factories, raw materials, etc.

For instance, let us say that the prevailing rate of interest which a man who saves his money can command is 3 per cent. This must mean that the profits which entrepreneurs can make by using this man's money must exceed 3 per cent. And where can these profits come from except from a more than 3 per cent reduction in costs effected by improved methods of production? So we come to the conclusion, which was certainly not apparent at first sight, that the very existence of a rate of interest must mean that investing is pushing down the costs of production just as steadily and continuously as saving is pushing down prices. This, say the professionals, is the root of the matter. The error of Mr. Hobson and the whole school of thought which attributes the occurrence of crises and slumps to over-saving is that they forget that saving and investing reduce costs as well as, and as much as, they reduce prices.

What are we to say of this ingenious analysis? Are the professional capitalist economists right again? As against Mr. Hobson's theorem, regarded as an adequate explanation of the occurrence of crises, I believe that they are. Their analysis does show that there is no inevitable reason why the existence of saving should drive prices below costs and so produce a crisis.<sup>1</sup>

If we accept the professionals' argument on this point, we shall be led to an important conclusion as to the effects of adopting the remedy of the "over-savings" school, *viz.*, the issue of sufficient new money and credits to maintain the prices of consumers' goods in spite of the existence of saving. We shall see at once that, if this is done, an ever growing gap must appear between the costs and the prices of consumers' goods. If the

<sup>1</sup> The reader will, however, be asking whether the introduction of improved and so cost-reducing methods of production is the only object of saving and investment. May not more producers' goods be needed, with which to produce more consumers' goods, even at existing costs, in order to satisfy new markets in, for instance, hitherto undeveloped countries? But this hypothesis involves the supposition, it will be noticed, that the prices of consumers' goods were above costs to start with: that demand exceeded supply in this department. In other words, this form of investing can only take place when the whole system is in a period of expansion; when there is a permanent unsatisfied demand for commodities at prices above costs of production. The elucidation of the vital differences between this sort of investing, which means an expansion of the productive system without any necessary change in the technique of production, and the form of investing which is only possible if it enables costs of production to be lowered, would anticipate the main argument of Part IV of this book.

active investors use the public's savings to introduce cheaper methods of production, they will be sending the costs of production down and down. But Mr. Hobson will be busy holding prices up. What will fill the ever growing gap between costs and prices? The difference between costs and prices is profits. Hence the maintenance of a stable price-level will produce, as savings are invested and costs fall, an ever mounting rate of profit.

It will in the end emerge that this is the real, though often unconscious, object of the whole policy. In the meanwhile, what is the professionals' objection to the maintenance of a stable price-level? The answer to this question will form the subject of Chapters V and VI. We can only say here that the professional capitalist economists are able to advance contentions which prove that the maintenance of a stable price-level for consumers' goods by the perpetual increase of the amount of money in circulation will set up disorders in the system which make the outbreak of a crisis inevitable. And, as we shall see immediately, a crisis actually did occur when such a policy was adopted in America in the nineteen-twenties.

In the meanwhile we may sum up our present conclusions. We have demonstrated that, in spite of its far greater plausibility, the over-savings hypothesis of Mr. Hobson can no more explain the occurrence of capitalist crises than can the "A+B" theorem of Major Douglas. The professional economists can demonstrate that there is nothing in the existence of savings which must in itself create crises. Moreover, they indicate that Mr. Hobson's remedy, of the maintenance of a stable price-level by an expansion of credits sufficient to offset the effect of savings on prices would produce—though, of course, far less rapidly and catastrophically—the same inflationary crisis as would Major Douglas' proposed deluge of new money. And here we catch sight of a suggestion of great importance. It is evident that Mr. Hobson's critics consider that *a stable price-level is itself, in modern conditions, when savings and technical progress are continually reducing the costs of production, a definitely, if esoterically, inflationary phenomenon*. They evidently suppose that such a policy will end in one of these overstimulations of industry which we call "a boom" and have

learned by painful experience to know as the immediate precursor of crisis.<sup>1</sup>

There exists another school of economic thought which advocates the same policy as does Mr. J. A. Hobson, but does so on different grounds. This school also advocates an issue of new money, or an expansion of credit, just sufficient to maintain, but not to raise, the general price-level. But it does not base its case on the need to offset the depressing effect on prices of the existence of savings.

Let us take the famous American economist, Professor Irving Fisher, as the spokesman of this view. We shall find, however, that this school is a very inclusive one. It includes, on the one hand, amateur economists who hold the milder type of under-consumptionist views and, on the other, some famous names amongst professional economists. For example, in addition to Professor Fisher, Professor Cassel must be placed in this category, and so, in the last analysis and in spite of many and subtle reservations, must be Mr. Keynes.

Indeed, it is not too much to say that this school of thought is to-day politically, if not intellectually, dominant. Its left wing of moderate under-consumptionists appear to dictate the monetary policy of the American Government. Its right wing of so called "stabilizers" appear to inspire the policy of the British Government. For both of these Governments have declared it to be their intention first to restore the price-level prevailing in 1929 or in 1926 (there are contradictory pronouncements on this point) and then to keep it stable. The importance of the views of this school cannot, therefore, be overestimated. Professor Irving Fisher, whom we take as its representative spokesman, has recently expressed the essence of his view as to the cause and cure of capitalist crises in a popular and readable little book called *Inflation?*<sup>2</sup>

The cause of crises is to be found, he tells us, in an unstable

<sup>1</sup> This view has an obvious application to the present (1934) situation in Great Britain. Sterling prices have been held stable. As we noticed in Chapter I, the profits of British industry were 30 per cent, 5 per cent, 18 per cent, and 27 per cent higher in the four quarters ending September 1934 than they were in the four quarters before that. The reader should compare this situation with the account given below of what happened in America in the nineteen-twenties.

<sup>2</sup> Allen & Unwin, 3s. 6d. Professor Fisher's larger volume, *Stable Money*, has unfortunately appeared in Britain too late for comment in these pages.

price-level. Hence the objective of a sane monetary policy must be the maintenance of a stable price-level. Any other policy will result in disaster. Rising prices and falling prices are equally inimical to social justice and economic equilibrium. In modern society, however, the total volume of production is continually increasing. Now this must result, unless the volume of money is also increased, in continually falling prices. This is, we see, precisely the same conclusion which Mr. J. A. Hobson reached. But Professor Fisher does not, like Mr. Hobson, think that prices will drop because of the existence of savings. Instead he bases his argument on what is called the quantity theory of money. The amount of money is said to balance, as it were, the amount of commodities. If there are 100 commodities on the market and £1,000 of money in circulation, the average price of each commodity will be £10. If now increasing production puts 200 commodities on the market, and no more money is forthcoming to buy them, the average price of each commodity must drop to £5. The only way to keep prices at the old level is to put 1,000 new pounds into circulation. Then there will be £2,000 of money to balance the 200 commodities and the price-level will be kept stable at £10 a commodity. Hence, Professor Fisher concludes, if you want to keep the price-level stable and so avoid crises you must continually expand the amount of money in circulation to the same extent that the production of commodities increases.

Here is a characteristic statement of the goal of monetary policy as Professor Fisher envisages it.

*“ If Money and Goods Were Geared ”*

“ What we need is that the money circulation (meaning its total effectiveness, which involves both volume and speed) shall be steadfastly *proportioned* to the fairly steadfast needs of business ; that is, we want to see the line for money moving *parallel* with this line for production. The ratio between the two would then be constant ; that is, if all the goods for a year increased 4 per cent, and the money to buy them with also increased 4 per cent, the average price (the price for a cross-section of the goods) would be the same as before. In other words, the *price-level* would be constant and really level.”

Dc

We see that Professor Fisher advocates the same action as does Mr. Hobson, *viz.*, a steady increase in the circulation of money, but that he gives a different reason for it. We have already seen that Mr. Hobson's policy would be likely to have very different results from those which he anticipates. And this conclusion is equally true of Professor Fisher's policy. For the reasons given to justify a steady increase in the " money circulation " cannot possibly alter its effect. If Mr. Hobson's policy is likely to result in inflation, a boom and then a crisis, so would Professor Fisher's.

We have not yet found adequate reasoning with which to support this conclusion. It is a conclusion, however, which can be verified from experience. For Professor Fisher's policy has been tried out upon the widest scale and under the most favourable circumstances. Nothing is more striking to the reader of *Inflation?* than to observe how Professor Fisher deals with this decisive practical trial of his remedy. Now Professor Fisher tells us that " every rise of the price-level is a boom, and every fall a depression." A stable price-level, on the other hand, he tells us, produces permanent stability and prosperity.

What, then, is our surprise to find that from 1921 to 1929, during the greatest boom in history, which was followed by the greatest crash in history, *the American price-level was virtually stable*. Strangest of all, this fact is clearly depicted by a graph presented by Professor Fisher on page 75 of his book :

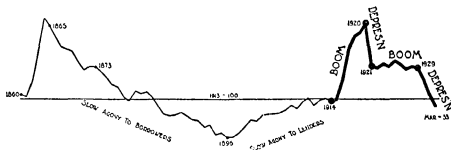


CHART 12. AMERICAN WHOLESALE PRICE HISTORY, 1860-1933<sup>1</sup>

The line across the Professor's graph is almost horizontal between 1921 and 1929. It will be seen that the 1921-9 period,

<sup>1</sup> Reproduced by courtesy of Messrs. George Allen & Unwin



the period immediately preceding the greatest of all crises, was the one period of virtual price stability which America has ever known.

Professor Fisher quietly ignores the fact that his graph destroys the argument of his text. His graph shows conclusively that a stable price-level does not prevent booms and crises. His graph reveals the fatal fact that its author's policy of "gearing money to production," of increasing, that is to say, the effective circulation of money in exact proportion to production, was tried out in America for eight years in ideal conditions—and ended in an unparalleled crisis !

Now there is nothing very remarkable in all this. Many economists have made mistakes before Professor Fisher (though it is true that not many of them have had the misfortune of having their policies adopted, and their errors exposed, so cruelly and on so gigantic a scale as were his). But what is remarkable is that after this conclusive trial Professor Fisher behaves exactly as if nothing had happened. He is to-day advocating this same policy, and is promising us brilliant results from its adoption.

Writing in April 1933, he advocates raising the American price-level to what it was in 1926 ; that is to say, by more than 70 per cent, and then stabilizing it.<sup>1</sup> He notes that as he goes to press his policy is being adopted by the new Administration of Mr. Roosevelt. Indeed, the debt which the whole New Deal owes to the Professor's thinking is too little realized. For many years now his views have been permeating American economic thought. Just as Mr. Hobson is the theoretical father of most British "progressive" thinking on economic subjects, so Professor Fisher is the only begetter of nearly all the economic theories of the American Liberals. To-day a whole school of younger American economists have, whether they realize it or not, his approach and outlook. And these are the men who now dominate the monetary policy of the Roosevelt Administration.

Hence it was no accident that in March 1933 Professor Fisher's

<sup>1</sup>One might have supposed that the logical course to be deduced from Professor Fisher's argument would be to stabilize the price-level immediately at whatever point it happened to be when his policy was inaugurated. It is noticeable, however, that nearly all "stabilizers" prefer an initial *raising* of the price level, and propose stabilization only subsequently. The reasons for this remarkable inconsistency will emerge in subsequent chapters.

policy of first raising the price-level and then holding it constant was officially adopted and has since been vigorously pursued. Here is what Professor Fisher promises to us from this second trial of his programme. He writes that if his programme is carried out it

“ will mark 1933 as perhaps the most important turning point in all economic history. Not only may we expect recovery from depression with a speed unmatched in any previous instance, but (assuming that reflation is to be followed by stabilization) we may expect a new economic epoch characterized by freedom from great depressions, because the monetary unit will be deliberately held constant.”

The human mind is assuredly more sanguine than rational. How else are we to account for the fact that not only Professor Fisher, but Mr. Roosevelt and all his supporters, can suppose that though the stabilization of the price-level in the nineteen-twenties resulted in the most disastrous crisis in history, a stabilization of the price-level in the nineteen-thirties will result in “ a new economic epoch characterized by freedom from great depressions ” ? As Marx, in his irascible way, said of Destutt de Tracy—“ There you have bourgeois idiocy in all its beatitude.”

The lessons of experience appear to support the view that an expansion of money or credit, no matter whether it be undertaken in order to offset savings, or in order to balance increasing production, results in an inflationary boom, which in turn produces a crisis. We have got an indication of why this is so in the case of an expansion justified as an offset to savings. Savings not only depress prices, they depress costs. Hence if their effect on prices is offset, the continuing fall in costs creates an ever growing gap between costs and prices. We have now seen that, naturally enough, the fact that the expansion of money is justified, not on the need to offset savings, but in order to balance increasing production, does not prevent the same inflationary consequences.

It looks as if increased production and decreased costs are merely two different ways of looking at the same thing : as if the one implied the other. And, in fact, once we think of it, it is

obvious that unless a depression already exists, and some capital and labour are consequently unemployed, the total volume of production cannot be increased except by reducing the costs of production. The only way in which we can get more commodities, if we are all already at work producing the existing supply, is to find some way of producing the existing supply with fewer workers, less electrical power and the like, so that some of these "factors of production"<sup>1</sup> may be freed for producing a new, additional supply of commodities. Hence the hypothesis of increasing production, upon which Professor Fisher bases his argument for more money, involves the corollary that costs are falling.

We are now in a position to appreciate why the most responsible capitalist economists take so grave a view of the monetary policy now being pursued in America. For not only are prices being prevented from falling with rapidly falling costs. The price-level is actually being pushed continually upward. Since March 1933 (the low point) the Irving Fisher index of wholesale prices has risen from 55 to 79·4 on January 5th, 1935. This means that American costs and prices are moving off in opposite directions! No wonder that there has been a sharp revival in profits. Profits are being expanded, as it were, in both directions. They are growing both as costs<sup>2</sup> fall and as prices rise.

The stage seems set for a new boom in profits.<sup>3</sup> But now the attempt is being made to engineer a boom by a financial policy far more obviously and crudely inflationary than was the policy pursued in the nineteen-twenties. If the outbreak of the 1929 crisis showed that the maintenance of a stable price-level between 1921 and 1929 was a subtle form of inflation, no one should mistake the forcing up of the price-level in 1933 and 1934, in face of rapidly diminishing costs, for anything but rapid inflation. And experience appears to demonstrate, although we have

<sup>1</sup> "Factors of production" is a term we shall be using continually. Let us, therefore, define it at once. It is simply a convenient, inclusive sort of phrase which means such things as labour, raw materials, tools, electrical power, land to put your factory on, and the like—everything, in a word, necessary to production.

<sup>2</sup> As we shall explain below only one kind of costs are falling in America. Costs are being driven down by technical improvements. This means in the last analysis that fewer men are needed to produce the same amount of goods. But another variety of costs—wage costs—the amount of money paid per hour of work—have not fallen, and may in some cases have risen.

<sup>3</sup> In the profits of a limited number of favoured corporations, however.

not as yet found an adequate rational explanation of this fact, that inflation invariably precipitates a crisis. It would be greatly to over-simplify the present American situation, however, to suggest that this is all. We shall be in a better position to examine the economics of the New Deal when we have completed this stage of our argument.

To sum up. Experience confirms the view of the best capitalist economists that a deficiency of money, which causes falling prices, is not the cause of crisis. These economists seem able to show that, on the contrary, dropping prices, accompanying dropping costs, are a necessary condition for any possibility of stability : that the maintenance of stable prices by the continual emission of new money is in modern conditions definitely inflationary, and so, apparently, conducive to crisis. They are thus able to demonstrate that the easy, pleasant, and generally acceptable solution of our troubles proposed in different forms by all the various schools which attribute the occurrence of crises to a deficiency of money would (and will) make matters worse instead of better. There is no possibility that the maintenance of a stable price-level by the provision of more money will prevent the recurrence of crises. On the contrary, just such a policy seems to have precipitated the last crisis, and may be expected to precipitate the next.

The most responsible and conservative capitalist economists emerge, then, triumphant over all their heterodox opponents. They are able to show that all the proposed remedies of the latter are founded on erroneous diagnoses, and would but exacerbate the disease (as they always have done whenever they have been tried). The disease, however, remains. We will now turn our attention to what the most responsible capitalist economists have themselves to say about the nature, cause, and cure of capitalist crises.

#### SUMMARY OF CHAPTER III

If crises do not occur, as Major Douglas supposes, because the system does not distribute enough money to buy all the commodities it produces, why do they occur? Mr. J. A. Hobson's

view. Crises occur because of the deficiency in consumers' purchasing power caused by savings. Savings, he proves, must push down prices. Savings, he alleges, will push prices below costs. His remedy is to offset saving by a gentle issue of new money which shall be just sufficient to maintain a stable price-level, and to minimize savings by an equalitarian redistribution of income.

The professionals' answer. Saving means investing. And investing reduces costs as much and as well as prices. How investing reduces costs. The prevailing rate of interest as a measure of the reduction of costs. The consequence of maintaining a stable price-level seen to be an ever widening gap between costs and prices. Profits are what fills this gap. Experience indicates that this condition is "a boom" and that it is followed by a crisis.

Stabilization of the price-level by the issue of more money as the specific against crisis. Professor Irving Fisher as spokesman. "Gearing money to production." Like policies produce like results, whatever their justifications. The lesson of experience. The fatal graph. American price-level stable all through the boom of the nineteen-twenties. The Professor learns nothing and forgets nothing. "A new economic epoch" without crises promised. The beatitude. Increased production and decreased costs seem to be associated. Professor Fisher as the grandfather of the New Deal. Inflationary character of the New Deal. Recapitulation of the breakdown of all theories which attribute the occurrence of crises to a lack of money.

## CHAPTER IV

### *Too Much Money? Dr. Hayek*

WE noticed in Chapter I that the main body of capitalist economic theory knows nothing of the occurrence of crises. We may cite Professor Robbins again upon this point. He begins his preface to the English translation of Dr. Hayek's *Prices and Production* with the remark, "The pure theory of economic equilibrium, the great achievement of nineteenth-century economics, provides no explanation of trade depression." And Dr. Hayek says himself that for the purposes of his analysis "we have to start where general economic theory stops: that is to say, at a condition of equilibrium when no unused resources exist. The existence of such unused resources is itself a fact which needs explanation." (Dr. Hayek, *Prices and Production*, p. 31.)

Naturally, therefore, most capitalist economists have very little to say about the subject. In their treatises, the occurrence of crises, if it is mentioned at all, is usually made to fulfil the rôle played in antiquity by the seven plagues of Egypt. As then the plagues fell upon Pharaoh because of his disregard of the prophecies of Joseph, so now the plague of crisis falls upon the capitalist world because of its disregard of the advice of the professors. Most capitalist economists maintain, that is to say, that there is nothing in the nature of capitalism which makes the occurrence of periodic crises, of the whole familiar cycle of boom, crisis, depression, recovery, boom, crisis, inevitable. It is merely that statesmen and business men, in their headstrong ignorance, refuse to listen to the professors and so damage the essentially perfect mechanism of the system.

Of recent years, however, the inadequacy of this explanation has become more and more apparent. It was always difficult to understand how the mistakes of politicians or business men could account for an approximately regular ten-yearly cycle of business expansion and contraction, or how they could produce an enforced idleness of available labour and capital. It was clear enough how such things as tariffs, subsidies, excessive taxation, monopolistically controlled prices, or mistakes in forecasting the

trend of demand, might reduce the standard of life which an undisturbed and perfectly functioning capitalism might be supposed to provide. It was easy to see how governmental or private mistakes might cause waste, might reduce, as the economists would say, the net income received by the community for a given amount of productive effort. But it was by no means clear how such mistakes could produce an enforced and ever recurrent idleness of a percentage of the factors of production. It was easy to see how tariffs or mistakes in business forecasting, for example, would result in a less economic employment of the factors than was possible. But how could such mistakes result in it being impossible to employ many of the factors of production at all? Mistakes, in other words, would easily account for our having to work harder for less pay than we should have had to do if no mistakes had been made; but how could they account for our being prevented from working at all?<sup>1</sup>

Such considerations, the growing urgency of finding relations for the proposals of the credit cranks, and, above all, the ever augmenting gravity of the crises themselves, have, as we noticed in Chapter I, induced at least some capitalist economists to attempt an analysis of the "trade cycle." But since the main *corpus* of their science demonstrated that the phenomenon which they desired to investigate did not, and could never, exist, they have been obliged to approach the subject by means of a kind of theoretical back door; they have been obliged to create a sort of economic "special subject," the relationship of which to the science itself can never be properly defined. And this special subject, by means of which capitalist economists can alone approach the phenomenon of crisis, is monetary theory.

A diagnosis of the intermittent fever of the system is, in effect, the object of Mr. J. M. Keynes' chief work, *A Treatise on*

<sup>1</sup> It is a failure to exhibit this distinction which makes, for example, the explanation of crises given by Mrs. Barbara Wootton in her recent book, *Plan or No Plan?* (pp. 130-50), unconvincing. Mrs. Wootton has to resort to the hypothesis of "an exceptional coincidence of mistakes" in order to account for periodic crises. Her eclectic summary of possible causes of crises is a good example of the views of capitalist economists not belonging to the particular school whose analyses we shall discuss in this chapter. (The fact that Mrs. Wootton happens to entertain socialist opinions of an ethical type does not prevent her being a capitalist economist, and a very competent one, in the precise sense which we have given to the term.)

*Money*, published in 1930.<sup>1</sup> It was not, however, until the following year that there appeared in English the most interesting capitalist attempt to describe and to account for the trade cycle. In 1931 the English translation of Dr. Hayek's *Prices and Production* was published. With the appearance of this little book a new comet swam into the ken of the Anglo-Saxon economists. They found themselves at last presented with a theory of capitalist crisis and of the trade cycle which made sense. We shall in the end find ourselves compelled by the facts of the case to reject Dr. Hayek's theory. A consideration of it will prove, however, quite the readiest method of penetrating more deeply into our subject.

In describing Dr. Hayek's theory we need not traverse what seems, in retrospect at any rate, the unnecessarily obscure presentation which he adopted in *Prices and Production*. Moreover, we have already made use of some of his conceptions in our review of under-consumptionist illusions. We shall now be able to take a good many propositions as established by the argument of the last two chapters.

In essence, then, Dr. Hayek believes that the existence of the trade cycle, containing within it the deadly stages of crisis and subsequent economic prostration, is due to the fact that the authorities in charge of the credit and money resources of the community *do* pursue the policy advocated by Mr. J. A. Hobson, Professor Fisher, and the adherents of their respective schools of thought. They do, that is to say, increase the amount of money in circulation sufficiently to offset the depressing effect of savings upon prices, as Mr. Hobson would put it, or to offset the growth of total production, as Professor Fisher would put it.<sup>2</sup> Thus Dr. Hayek's school of thought attributes the occurrence of crises to exactly opposite causes to those indicated by all varieties of the under-consumptionists. The under-consumptionists think that we save too much; this school thinks that we save too little.

<sup>1</sup> In this work Mr. Keynes elucidated very fully the question of the proportion maintained between saving and investing, which we have raised in the last chapters. But he discussed it from a different point of view. He was interested in showing that the effect of *not* expanding credit might be to make saving exceed investing: to make saving turn into hoarding. And if this occurred, unemployment would result, he was able to show. For the consumers' goods department would be shrinking while the producers' goods department would not be growing.

<sup>2</sup> "It was not old-fashioned practice but new-fashioned theory which was responsible for the American disaster." (Professor Robbins, *The Great Depression*.)



The under-consumptionists think that the financial authorities issue too little money ; this school thinks that they issue too much. The under-consumptionists accuse the bankers of ruining us by deflation ; this school accuses them of ruining us by inflation.

Dr. Hayek begins his description of the trade cycle at the point when economic activity is improving *into* a period of recovery, *from* a period of acute depression following a crisis. He believes that at this point certain fatal steps are taken by the financial authorities which foredoom the system to subsequent crisis and collapse.

We must assume a revival in economic activity. We shall come round again to this point in the cycle, and our last task will be to show how this revival takes place. Our present task is to show how and why (according to Dr. Hayek) this revival, instead of leading to "the state of equilibrium"—that blessed but illusive Nirvana of the capitalist economists—always leads to boom and then to crisis and collapse. Now it will be clear from the argument of the last chapters that such a revival will soon begin, unless something is done to offset its effects, to reduce prices. Looking at it in Professor Fisher's way, we may say that as the revival is increasing production, it must, if the amount of money in circulation is not increased, be reducing prices. Looking at it in Mr. Hobson's way, we may say that the savings which are being made must be reducing prices. But, says, Dr. Hayek, the new investments will also be reducing costs. Therefore the reduction in prices will be perfectly healthy ; there will be nothing in it, that is to say, which should check a steady stable, if slow, process of revival. For the fall in prices will be only proportionate to the fall in costs : there will be no tendency to drive prices below costs.

The financial authorities have never and are never likely, however, to take this view. They will notice the tendency for prices to fall : they will remember that the slump, which is very fresh in their memory, "was caused by falling prices." They will regard any "weakness," as it will be called, in prices as a danger signal. The voice of Dr. Hayek, who will be pointing out that costs are falling and that accordingly there is nothing wrong with falling prices, will be but still and small. Moreover,

the financial authorities will find that, undeniably, the renewed tendency to a fall in prices is limiting recovery. If prices could be increased, or, at any rate, kept stable, recovery would be made more rapid. For the "weakness" of prices is limiting profits. Falling costs of production would be causing, the authorities will realize, the most splendid profits if only prices could be prevented from falling also.

Moreover, the financial authorities will be in a position in which they undoubtedly can, if they like, prevent the fall in prices. They will have regained great "liquidity"; the banks, that is to say, will be in a position to lend freely. There will be willing borrowers at the very low rate of interest which will have been inherited from the period of acute depression from which the system is emerging. Will it not seem clear to everyone, to statesmen, practical bankers, and monetary theorists alike, that the more money is lent out, the quicker recovery will come, the more unemployment will be reduced, and the more profitable will industry be rendered? It is at this point, Dr. Hayek believes, that an act of economic original sin is invariably committed. The bankers do lend freely and cheaply. They keep down the rate of interest even after the demand for loans has begun to revive. Surely, they feel, it would be a crime to "nip the revival in the bud," by making money dearer?<sup>1</sup> The bankers pride themselves on their public spirit in lending so cheaply (and, of course, it enables them to lend more). Moreover, even if the bankers, still bruised from the last collapse, are timid, the Government, desperately anxious to revive employment, will actually put pressure upon them to increase and cheapen their loans.<sup>2</sup> In extreme cases the Government may even go into the banking business itself in order to "distribute purchasing power," as the process will be called. The revival will soon become more and more marked.

But alas! Dr. Hayek believes, there is a fatal, though unseen, limit to the amount of money which can be lent without sowing the seeds of new catastrophe. This limit can be defined in several ways. We may say that the financial authorities must not lend

<sup>1</sup> *Vide* the almost universal propaganda for the continuance of "cheap money" which is being conducted in England in 1934, in spite of the pronounced revival of business activity.

<sup>2</sup> For the extreme example of this process *vide* America 1933-4.

so much money that their loans will result in an increase in the extant amount of money of all kinds. Again we may say that they must not lend out more money than they are entrusted with: they must not lend more money than the public has saved. In other words, they must not allow the amount being currently invested to exceed the amount being saved. These two prohibitions are, it will be seen, different ways of saying the same thing. For if the financial authorities lend, or invest, more money than the public saves, the difference—the margin of money invested over money saved—must come from somewhere. It must be new money created by the bankers or the Government.

The temptation to increase the circulation of money is the more difficult to resist in that there need be no question of any crude printing of money. By "money," Dr. Hayek is careful to point out, he means every kind of credit instrument which can be used to mediate the circulation of commodities.<sup>1</sup> Hence the principal way in which the bankers "increase the circulation" (by which Dr. Hayek means the total amount of money extant) is simply by failing to raise their rate of interest. For there is (if only it were discoverable) some particular rate of interest at which the demand for new loans would be kept down to the amount of money being saved by the public. Thus all the bankers need do, in order to cause an increase of the amount of money in circulation, is to keep their rate of interest below this rate. (We shall see below the extreme difficulty of discovering what this rate is.) Moreover, as we know, this new money need not raise the price-level at all. It may merely offset the tendency of the price-level to drop. A rise in the price-level, however, is popularly supposed to be the indispensable indication of inflation. Thus the financial authorities may be briskly inflating; and yet they may believe with a clear conscience, and the endorsement of many professional economists, that they are doing nothing which even savours of inflation.

<sup>1</sup> It is important to realize the great width of Dr. Hayek's definition of the term "money." He means by money all those forms of circulatory media, such as bank deposits circulated by cheque, commercial bills, overdraft facilities, bank loans, or even accommodation extended from one firm to another, which are generally called credit. Thus for Dr. Hayek there is no relevant difference between an expansion of credit and the simple printing of new banknotes,

But what, according to Dr. Hayek, will be the consequences of this subtle form of inflation? We know the answer to this question already. For this is just the policy advocated by Mr. Hobson and Professor Fisher. The expansion of credit will create enough new money to offset the "sag" in prices due to the existence of savings. But costs will be steadily reduced by the new processes made possible by the savings. Hence profits, which are the difference between costs and prices, will be continually augmented. We have seen that experience teaches us the painful lesson that there is a limit to this upward movement, and that when that limit is reached, not only must the upward movement stop, but a sharp downward movement must begin. A boom, that is to say, never flattens itself out into a period of stable prosperity, but always ends in a crisis. We must now enquire into why this should be so.

At first sight it would seem that the obvious limit to the upward movement is when all the factors of production have become employed in one department or the other. For the effect of the new money being "injected into the system" (the phrase is Dr. Hayek's) by the expansion of credit is to augment the demand for factors of production in the producers' goods department without decreasing the demand in the consumers' goods department. Hence no factors will be freed from the consumers' goods department. Accordingly so soon as all the factors of production are working again in one department or the other, no increase in the amount of money in circulation will enable the producers' goods department to expand. For the only way in which the producers' goods department can get hold of more factors of production is for them to be freed by the consumers' goods department. And this can only happen by allowing savings to depress the consumers' goods price-level, to curtail demand in that department, and so to free factors of production.

But stay: is this voluntary surrender of factors by the consumers' goods department the only way in which the producers' goods department can acquire them? No, it is not. There is a method by which one department can steal the factors of production from the other. And this method is precisely the "injection," as Dr. Hayek calls it, of new money into the system.

It works thus. If the bankers inject new money into the producers' goods department, it will enable this department to turn robber; it will enable it forceably to remove factors of production from the consumers' goods department, although this department has not voluntarily released a single worker or a single unit of electrical power—to exemplify two particular factors. For the new money, as soon as it has got into the hands of the capitalists who make producers' goods, gives them the power to bid higher for these factors than before. Hence the consumers' goods department will see its labour supply, etc., being drawn off. The proportionate size of the producers' goods department will grow just as it would if adequate voluntary savings were being made.

Well, then, what is wrong with that? The only difference between obtaining the money for investment from savings, and injecting new money seems to be that in the former case the growth of the producers' goods department at the expense of the consumers' goods department is the result of a voluntary agreement between them, while in the latter case it is the result of the *force majeure* acquired by the producers' goods department by its possession of new money. Why should not the boom be kept up indefinitely by injecting more and more money into the producers' goods department, and so continually forcing the consumers' goods department to contract sufficiently to hand over the necessary factors of production? This would amount to forcing the public to save enough to cover this rate of investment. (Mr. Dennis Robertson has coined the term "forced savings" to describe this process.) The answer is—and this is Dr. Hayek's essential point—that these "forced savings" do not have the same effect as voluntary savings. If you inject new money, and so give the makers of producers' goods, the power to steal factors from the makers of consumers' goods, you will have committed an unforgivable economic crime and the fearful retribution of crisis and collapse will surely fall upon you.

Nor is it difficult for Dr. Hayek to show why this is so. He has only got to direct our attention to the subsequent history of the new money which the bankers have injected into the economic system by lending it to the capitalists who make

producers' goods. What happens to this money when the capitalists have spent it? They spend it on wages, on rent, on paying for raw materials, etc., etc. It goes then, some of it directly, some of it indirectly, into the hands of individual consumers. And what do these consumers do with it? Dr. Hayek's allegation is that they spend it—or almost all of it. But if they spend it, they will spend it on consumers' goods. In other words, this new money, after first increasing the demand for producers' goods, and so for factors with which to make producers' goods, will now, and equally, increase the demand for consumers' goods, and for factors with which to make them.

This is the revenge of the consumers' goods department. The producers' goods department cannot, as it were, retain its new money: it inevitably trickles through into the consumers' goods department. The new money gives the producers' goods department only a temporary advantage. Before very long it has percolated into the hands of individual consumers, who use it to reinforce the consumers' goods department. The relative advantage of the producers' goods department is lost. The stolen factors of production are pulled back into the consumers' goods department. It is soon a case of pull devil, pull baker between the two departments. The inflationary possibilities of this situation are obvious. For the struggle between the two departments is conducted by first one and then the other using new money to bid up the price of the factors of production. It begins to be apparent that the upward movement will only go on so long as ever new doses of new money are injected into the system. For once the stream is stopped the consumers' goods department will soon have got all the new money. The producers' goods department will be decisively defeated.

Yet this process would hardly be sufficient, in itself, to account for the recurrence of crisis. The main symptom of every crisis is, we recollect, the existence of a mass of idle factors of production, particularly concentrated, it is noticeable, in the producers' goods department. In order to account for this phenomenon, Dr. Hayek introduces the conception of what he calls "specific" and "non-specific" factors of production. A

non-specific factor is a mobile factor, such as, for example, unskilled labour or electrical power, which can be used in either one or other department of production. A specific factor is a non-mobile factor, such as a blast furnace or a machine tool for turning out, say, cylinder blocks for motor-cars—factors which by their nature can only be used in one department of production. Moreover, Dr. Hayek says, our concept of two departments of production is an over-simplification. The truth is that there is a whole hierarchy of departments of production—ranging from putting the finishing touches on, and selling, motor-cars, to making the machine tools, to make the blast furnaces, to make the steel, to build the factories, to make the motor-cars. Dr. Hayek calls this industrial house that Jack built “the structure of production.” So when we talk of pulling factors of production from the producers’ goods department to the consumers’ goods department, he talks about pulling them *down* the structure of production—*i.e.*, from the producers’ goods end to the consumers’ goods end.<sup>1</sup>

Now we come to the point of his distinction between specific and non-specific factors. Take the situation when the consumers’ goods department begins to get hold of the new money and to use it to recover factors which it had lost to the producers’ goods department. The non-specific, mobile factors come back. But the specific, non-mobile factors, which have come into being in the producers’ goods department, cannot move down. New blast furnaces, new machine tool plants have been built. But now the shift in demand away from a demand for pig-iron, for example, and towards a demand for silk stockings, makes it more profitable to employ the available non-specific, or mobile, factors (the available electrical power and unskilled labour, for instance) upon turning out silk stockings instead of pig-iron. And so the blast furnaces must be damped and their complement of decidedly “specific,” or non-mobile, skilled workers must become unemployed. In other words, a whole quantity of specific, non-mobile factors of production *get stranded* in the producers’ goods department. They are left high and dry, unusable because their necessary complement of non-specific, mobile factors has

<sup>1</sup> “Down” the structure of production because he represents that structure as a triangle, the base representing the consumers’ goods end, the apex the producers’ goods end.

been drawn away from them by the renewed pulling power of the consumers' goods department.<sup>1</sup>

This conception of specific and non-specific factors explains a good deal. This "stranding" of specific factors in the upper reaches of the producers' goods department is, after all, much what might have been expected to happen if you tried to invest more money than you had saved. You tried to make people save more than they were willing to do. For "saving" is, precisely, postponing present consumption in order to enjoy increased consumption per unit of effort later. Hence if you try by monetary manipulation to get hold of more factors for investing in the producers' goods department than people are willing to release by saving, the unwilling savers have their revenge on you. You may easily manage to get away with your theft of factors to begin with. But as the new money, by means of which you have lured the factors away, gets into the consumers' hands, they rudely interrupt your process of investing in producers' goods. Your new blast furnaces may be only half finished, or maybe they are finished and have produced the steel for your new factories, but the new factories are not yet in production, when along comes the new demand from the consumers' goods department and pulls all your workers, etc., away again. And so your half finished factories and your finished, but now unusable, blast furnaces are left on your hands. If you could have had time to complete the process and have got the new factories into production you could have met the renewed demand for consumers' goods. But you were caught between wind and water and so had to give up the attempt to create the new productive methods.

This is the outline of Dr. Hayek's answer to the question of why our periods of recovery always turn into booms, which in turn collapse into crises. Let us summarize his views. Dr. Hayek considers that any recovery which is assisted by an increase in

<sup>1</sup> Mr. Keynes, as it seems to me, was very near to an elucidation of this point in his *Treatise on Money*. He pointed to a sudden shortage of "working" as opposed to "fixed" capital as the proximate cause of the end of a boom and the onset of crisis. By working capital he implied just these non-specific or mobile factors of production—labour, electrical power, and the like. By fixed capital he meant specific factors. Thus it is possible to say that the crisis is caused by the drawing off by the consumers' goods department of so much working capital from the producers' goods department that the operation of that department's fixed capital becomes impossible.



the circulation of money, as recoveries always are, must sooner or later result in a boom and then a crash. For the new money will set the two departments of production bidding against each other for factors. First the new money increases the demand of the producers' goods department without decreasing the demand of the consumers' goods department. Then it percolates through to the consumers' goods department and begins actually to increase the demand in this department. As soon, in other words, as the new money has got through to the individual consumers there will be an increased demand for immediate consumable commodities. And this demand will interrupt the process of production in the producers' goods department.<sup>1</sup>

But, it may be objected, cannot the consumers' goods department's counter-pull be counteracted in some way? Yes: it can be (and usually is) counteracted for a time by the issue to the producers' goods department of still more new money. For if this is done the producers' goods department will be once more enabled to outbid its rival. And experience shows that the recovery and the subsequent boom do go on so long as ever renewed doses of new money are enabling this to happen. *But each dose of new money must be larger than the preceding one.*

#### SUMMARY OF CHAPTER IV

Crises seen by the capitalist economists as punishments upon the world for not taking their advice. Crises, they say, are due to mistakes. It is easy to see how mistakes could make us have to work harder for less pay, but how do mistakes prevent us from working at all? Dr. Hayek and his crisis analysis as a new

<sup>1</sup> The reader will, no doubt, find this argument very paradoxical. Can it really be, he will object, that crises are caused by there being too *big* a demand for consumers' goods? Is it not obvious, on the contrary, that crises are caused, as the under-consumptionists rightly say (however useless their remedies may have proved) by there being too *small* a demand for consumers' goods to keep the wheels of industry turning? This common-sense objection is, in one sense, quite correct. We shall find that the real truth of the matter is that consumers' demand is too big for one purpose and too small for another: that Dr. Hayek is right in saying that you will only make the trouble worse if you increase it, and that the under-consumptionists are right when they say that anyhow you will make the position impossible if you diminish it. In other words, we catch here our first glimpse of the basic dilemma in which the capitalist system now finds itself. The full elucidation of this dilemma is directly or indirectly the subject of the whole of the rest of the argument of these pages.

comet swimming into the ken of Anglo-Saxon economists. Dr. Hayek ascribes crises to exactly opposite causes to the under-consumptionists. His account of the trade cycle. Overlending as economic original sin. "The injection of new money" possible without raising the price-level. Concealed inflation. Inflation as the theft of factors by the producers' goods department. The nemesis of this theft. Percolation of the new money from the producers' goods department to the consumers' goods department. The revenge of the consumers' goods department. Specific and non-specific factors. Flight of non-specific factors to the consumers' goods department strands specific factors in the producers' goods department. The attempt to establish the new, improved, but more elaborate methods of production interrupted by the renewed pull of the consumers' goods department. Recapitulation. Necessity of ever increasing doses of new money in order to sustain an inflationary movement.

## CHAPTER V

### *Too Much Money ? (continued)*

WE reached at the end of the last chapter an important and serious conclusion. We saw that Dr. Hayek asserted that once an inflationary movement has begun each new dose of money which is injected into the system must be bigger than the preceding one. For each dose that is squirted into the producers' goods department has to counteract, if it is to be successful in enabling that department to retain its non-specific factors, all the preceding doses of new money which have by now percolated through into the consumers' goods department.

This point is so important that we must demonstrate it quantitatively. Let us think of a capitalist economy in which £18 million of money measures the total demand in the producers' goods department and £2 million measures the demand in the consumers' goods department. This means that £18 million of money is circulating in the producers' goods department and £2 million is circulating in the consumers' goods department. For simplicity's sake we will assume that this community is static, *viz.*, that it saves nothing, or rather that it saves only enough to maintain, but not to add to, its stock of producers' goods. Now let us suppose that inventions begin to be made. The bankers of the community are anxious to put them into operation. The citizens cannot, however, be induced to make any savings which might provide the money to build the necessary plant. Accordingly the bankers create £2 million of new money and lend it to the inventors, thus enabling them to start offering wages to workers, to buy land and building materials, etc., etc.

Now the monetary position of the community has altered as follows : There will now be £20 million in the producers' goods department and still only £2 million in the consumers' goods department. It is clear that the producers' goods department, thus reinforced, will be able to pull away some workers (by offering them higher wages) and some other factors of production from the consumers' goods department. For its relative weight, as against its rival, will have increased. And what matters is the

proportion between the amount of money in each department. The absolute amount of money in each department makes no material difference. The position, that is to say, is the same if there is £20 million in one and £2 million in the other, or £40 million in one and £4 million in the other, or £1,000 million in one and £100 million in the other, if the proportion is always 10-1. For all that the absolute amount of money in circulation in a community determines is the absolute height of the price-level. And there is universal agreement that the absolute height of the price-level, so long as it does not move in either direction, makes not the slightest difference to anyone.

The inventors, then, equipped with £2 million of new money, will be able to begin building their factories. But what will happen next? As soon as they have half built their plants and spent half their money (*viz.*, £1 million), £1 million of new money will have got into the hands of the individual consumers. Now what, asks Dr. Hayek, will the individual consumers do with this new money? They will certainly spend it, for, remember, their purchasing power had been reduced by the initial theft of factors of production which the £2 million of new money had enabled the inventors to perpetrate. The consumers had been forced to "save," to reduce, that is to say, their standard of life; for their incomes had remained the same and the inventors had bid up the prices of everything with their new money. Hence when this new money gets into the consumers' hands it merely enables them to restore their old standard of life.

Now what is the monetary position of the community when the first £1 million of new money has got through to the individual consumers and is spent by them? The position will now be £19 million in the producers' goods department and £8 million in the consumers' goods department. The amount of money in each department, we repeat, measures the strength of the demand from that department. Hence what matters is not at all the absolute amounts in each department, but the proportion between them. The original proportion was 18 to 2 or  $\frac{9}{1}$ . Then when the new money was issued to the inventors the proportion became 20 to 2, or  $\frac{10}{1}$ . But the final proportion which has been established by the percolating through of half the new money to the consumers' department is 19 to 3. *The money in the*

*consumers' goods department has become a larger proportion of the money in the producers' goods department than it was immediately after the issue of the new money.* For to start with the proportion was  $\frac{2}{13}$ , or  $\cdot 11$  recurring. Immediately after the issue of new money it became  $\frac{2}{20}$ , or  $\cdot 1$ . Finally, after half the new money has got into the consumers' goods department, it has become  $\frac{3}{16}$ , or  $\cdot 156$ . The proportion of money in the consumers' goods department has gone up from  $\cdot 1$  to  $\cdot 156$ .

Moreover we observe that there is now actually a higher proportion of money in the consumers' goods department than there was originally, before the attempt was made to strengthen the producers' goods department by giving it the £2 million of new money. Originally the consumers' goods department had only  $\cdot 11$  of the money of the community. Now it has got  $\cdot 156$ .

This, however, is appalling. It means that the inventors will be unable to go on building their plants. They will be quite unable to go on outbidding the consumers' goods department. On the contrary, the £3 million now in that department will pull their workers and other non-specific factors back again to their old tasks of making consumers' goods. The inventors will experience this process by a sharp and unexpected increase in the prices of everything necessary for their work. All their estimates will be thrown out. They will find it quite impossible to complete their plants. They will have to go back to the bankers and say that they are very sorry, but that owing to the totally unforeseen rise in prices they must have some more money.

How much money will they need ? We have seen that at first the extra £2 million given to the producers' goods department created a ratio of 10 to 1 between the departments. Hence it will evidently be necessary to maintain this proportion between the money in each department if the process of expansion is to go on. For otherwise the advantage will swing over to the consumers' goods department and expansion will again become impossible.

The first thing, then, which the bankers must do is to restore this 10 to 1 proportion between the money in the two departments. How much new money will now be needed to effect this purpose ? The proportion has now become 19-3. Therefore it will now be necessary to add enough money to the producers'

goods department to convert this into a 10 to 1 ratio. But as there are now £8 millions in the consumers' goods department, a 10 to 1 ratio in favour of the producers' goods department can only be achieved by bringing up the money in that department to £80 million. It stands at £19 million. So no less than £11 million of new money must now be issued to enable the process of expansion to continue.

And now, of course, we shall observe what happens when half this second dose of new money has been spent and so has passed into the consumers' goods department. Immediately after the second dose the position is £30 million in the producers' goods department and £8 million in the other department, or a proportion of .1 in the consumers' goods department. After £5½ million of this new money has been spent the proportion becomes £24½ million to £8½ million, or  $\frac{8.5}{24.5}$ , or .34. The consumers' goods department has gained an unprecedentedly high proportion of the community's money. Drastic measures will have to be taken if the expansion is to continue at all—or, *indeed by now if a contraction of the producers' goods department to a size far below its original one is to be avoided.* How much new money will now be needed to restore the necessary 10 to 1 proportion? There are now £8½ million in the consumers' goods department, so that the money in the producers' goods department must be raised to £85 million in order to restore the 10 to 1 ratio. There are £24½ million there already, so £60½ million of new money must now be issued.

And so on and so on. The doses of new money which are necessary to sustain the expansion become rapidly larger. Naturally the process would not be likely to work quite as fast as in our purely diagrammatic example. For we have assumed for simplicity's sake (a) that the community makes no voluntary savings,<sup>1</sup> and (b) that the inflationary process is started with the massive dose of £2 million of new money—massive, that is to say, for a little economy with a total circulation of only £20 million. Again, of course, the injection of new money would not be likely to occur in distinct successive doses such as we have

<sup>1</sup> Voluntary savings are, we now see, the one way of getting money out of the consumers' goods department once it has got there and giving it to the producers' goods department, thus improving the latter's relative strength without having to make an addition to the total of money in circulation.

postulated for purposes of comparing their magnitude. It would be much more likely to proceed by a steady but ever more rapid flow of new money. Still the simplifications we have adopted do not affect the argument.

What we have shown so far is (a) that, in order to maintain a process of expansion, started, not by an increase in voluntary saving, but by a dose of new money, ever larger and larger doses of new money are necessary. And (b) that if and when this process of inflation is stopped the situation does not remain what it was after the last dose of new money has been administered: *nor does it even revert to what it was before the first dose was given*: it becomes far "worse," in the sense of far more prohibitive of any possibility of expansion, than ever before.<sup>1</sup>

Here, then, is the outline of an answer to our question of why an inflationary movement must produce a crisis as soon as it stops. An inflationary movement turns out to be merely a special method of expanding the producers' goods department at the expense of the consumers' goods department. But it is a method which has the fatal defect that the minute its application, on an ever increasing scale, is stopped it has the contrary effect, *viz.*, it enormously strengthens the consumers' goods department at the expense of the producers' goods department.

But we have not yet suggested any reason why the inflationary process should be stopped. Why, we naturally ask, should we not go on and on injecting ever larger doses of new money into the system? If this will perpetuate the boom, why, then, what is wrong with it? Nor is it adequate to tell us that it leads to an endless, limitless and ever more rapid rise of the price-level: that it leads to what Mr. Durbin, for instance, calls alarmingly "a high inflation." For what, we may answer, is the matter with "a high inflation," if only it perpetuates boom conditions? We cannot be frightened off by a name.

Reflection will make us admit, however, that it is impossible indefinitely to continue an ever accelerating increase in the issue of money, an ever mounting, and ever more rapidly mounting,

<sup>1</sup> We see also that, according to Dr. Hayek, a process of expansion, by which he means a recovery or a boom, is a relative growth of the producers' goods department at the expense of the consumers' goods department. It is not until the end of Part IV that we shall see clearly just what Dr. Hayek means by this and be able to appreciate the sense in which his opinion is correct.

price-level. Such a policy logically pursued to its conclusion, as it actually was by the German Government in the nineteen-twenties, comes to an end when the price-level is rising so rapidly that money has ceased to be an effective means of payment. But, we may still object, and here we return to an important point, there is no question of continuing our injections of new money until this disastrous condition has been reached. There is an obvious point, it is claimed, at which every sane inflationist or "reflationist" will stop. *And that is the point at which all the factors of production are employed in one department or the other.* Dr. Hayek's analysis, we are told, may be correct on the hypothesis that all the factors are employed. In that case, no doubt, it is true that one department cannot increase its production except at the expense of the other. Nothing, however, is more notorious than that in the early stages of recovery by no means all the factors are employed. Why not therefore inject new money into the system until the point of full all round employment has been reached? Then when you stop you will be able to "stabilize prosperity."

This plausible line of reasoning overlooks, however, the nature of Dr. Hayek's case. As we have seen, Dr. Hayek's contention is that once you have injected new money, once, that is to say, you have allowed investment to exceed savings, you will have a crash at whatever point of the upward movement you stop. You will have your crash if you stop before all the factors are employed, if you stop at the point at which they are all employed, or after the two departments have begun bidding against each other. For once you stop the injections of new money the rate of investment must drop to the rate of voluntary saving. Demand in the producers' goods department suddenly collapses. There is a sudden shift in the relative strengths of the pull of demand from the two departments. The pull shifts from the producers' goods department to the consumers' goods department. Accordingly, it becomes less profitable to employ men in making pig-iron than it is to employ them in making silk stockings. Soon it becomes flatly unprofitable to employ them in making pig-iron (in making producers' goods, that is to say). Then the blast furnaces will be damped, no matter whether during the previous period all the factors had been employed or



not. It is this sudden shift in the direction of demand, which must occur when the supply of new money to the producers' goods department dries up, and when all the previous supplies are swelling the demand in the consumers' goods department, which does the damage. The productive system cannot possibly adjust itself to this sharp tug of demand from a new direction. It has been built up during the boom to meet one type of demand. It cannot now suddenly change over to another. Or, rather, it can only change over by means of the convulsion which we call a crisis. We may think of demand as the wind which blows the ship of production along. The change in the direction of demand which must follow the cessation of an issue of new money is, then, like a change of wind so sudden that the ship of production inevitably jibs. Quantities of specific factors are bound to be left high and dry in the producers' goods department ; mass unemployment, etc., is bound to appear. The only thing which is true is that the higher you force the boom by means of continual injections of new money, the more shattering will be the crash when at length you have to stop.

It is partly, at any rate, a failure to grasp this aspect of Dr. Hayek's reasoning which makes many of his critics feel that his thesis is somewhat unreal.<sup>1</sup> Dr. Hayek seems to suggest that the crisis and slump are inevitable because a shortage of the factors of production makes it impossible both to carry on the existing scale of production in the producers' goods department and to meet a demand for consumers' goods undiminished by voluntary savings. And all this seems very remote from present day reality, with its chronic and long continuing superabundance of unemployed factors. His critics point out that all the factors of production are used at the peak point of a boom alone, if then. Moreover, as in Britain in 1929, a crisis often comes before all the factors of production have been brought into use. Dr. Hayek's picture must, however, I think, be understood as depicting the "real" elements in the situation, which must precipitate crisis if the financial authorities persist in a policy of the "expansion of credit," of "stabilizing the price level," or, as he so harshly calls it, of "injecting new money into the system."

<sup>1</sup> Even Mr. E. F. M. Durbin, a critical disciple rather than a critic, does not appear to me to have wholly appreciated this point.

It is the merit of his argument that it shows why the crash must in the end arrive, however long the bankers postpone it by injecting more and more money. But it is not suggested that all upward movements, based upon the false foundations of credit expansion, do in fact go to the ultimate condition of full employment for all the factors of production, to a contest between the departments for factors, and so to an ever more rapid bidding up of the price-level. On the contrary, most upward movements are arrested before this point. Purely financial considerations intervene. In other words, the bankers lose their nerve. They know from experience that, if they go on saving the situation by ever larger doses of new money, the crash, when it does come, will be all the worse. The rule of thumb regulations which they have made for themselves as to the proportions between cash and deposits, etc., begin to restrain them. (Although appropriate expansion by the central banking system can always, as it did in America in the nineteen-twenties, abolish this restraint.)

Usually, though not always, the bankers "flinch" before the boom has gone to its utmost real limits. They begin to draw in their horns and to restrict credit. Nor, of course, do they guess that in so doing they will bring the whole paper house of cards down upon their heads. They suppose that they will merely check the "unhealthy," "hectic," pace of the expansion, that they will restore a more orderly, if slower, rate of progress. But, as we are now in a position to see, the moment that they cease to inject larger and ever larger amounts of money into the system, thus enabling the producers' goods department to keep ahead of its rival, the balance will swing violently the other way. The consumers' goods department, reinforced with all the previous injections of money which have now percolated through to it, will gain a decisive advantage. The direction of the pull of demand, which the system must obey, will change abruptly. The producers' goods department will be drained of non-specific factors. The crash will come.

These considerations explain the fact that the crash usually appears to be precipitated by the wilful action of the banks in restricting, or, at any rate, ceasing to expand, the circulation. Mr. Hawtrey, Mr. Keynes, and others had given us, before Dr. Hayek appeared, an account of all this. They showed just how

the crash came and they, usually, implied that the bankers had no option but to precipitate it in this way. Their explanations, being purely monetary, never quite carried conviction, however, since they failed to show why the boom should not have gone on for ever if only the bankers had not lost their nerve—if they had been willing to break their rules about cash and credit ratios and had simply issued more and more money. The merit of Dr. Hayek's analysis is to have shown in terms not of money, but of real commodities, both why it is impossible to stabilize boom conditions by the cessation at an appropriate point of the issue of new money, and why it is impossible to continue indefinitely to issue bigger and ever bigger quantities of new money. But it is also this which gives his analysis its air of unreality. For it is a picture of what would happen if things were pushed through to the bitter end, rather than of what does happen in practice.

We have now accomplished the main part of our task. We have seen why it is, according to Dr. Hayek, that booms, based, as they always have been, on injections of new money, on a rate of investment in excess of savings, come to such indescribably bad ends. The phases of the rest of the cycle follow naturally. After the crash there is a period of acute economic prostration. The "stranding" of quantities of non-specific factors of production in the producers' goods department produces a secondary depression in the consumers' goods department itself. For millions of workers are without wages, thousands of capitalists without dividends. There is no need to describe here the disastrous and far-reaching reverberations of the crisis. They are easy to understand once we have accounted for the initial crash in the producers' goods industries. A crisis is, then, on this view, the convulsive attempt of the system to readapt itself to a changed pull of demand. And this adaptation is convulsive and periodic, instead of smooth and perpetual, because the true character of demand has been obscured by the issue of new money during the boom and recovery. What the bankers did when they allowed the monetary circulation to increase was, in effect, to make it seem that there was a much bigger demand for producers' goods in proportion to the demand for consumers' goods than there really was. (This is only a way of saying that they made it

appear that people were saving more and spending less than they really were.) Sooner or later the financial authorities have to drop this pretence. But the unfortunate productive system has been built up in obedience to a falsified and distorted pull of demand. The violent readaptation of a crisis has become inevitable.

After a crisis a period of depression sets in. How does it eventually lift? It lifts, says Dr. Hayek, by production getting going again on the simpler, more direct, more laborious methods which are what the real ratio of saving to spending demands. Demand, remember, has collapsed in the producers' goods department. The consumers' demand still exists—though in all severe crises it, too, is affected, as we have seen, by secondary reactions. Gradually non-specific factors are moved down the structure of production from the upper reaches of the producers' goods department towards the consumers' goods department. Specific factors are simply scrapped. The new, "shorter," structure of production, with its smaller producers' goods department and bigger consumers' goods department, begins to take shape. A crisis is, Dr. Hayek tells us, "a transition to less capitalistic methods of production." A crisis is, that is to say, the reconstruction of the productive system so that it shall possess a smaller producers' goods department and a larger consumers' goods department. The capitalists begin to find that it is profitable to employ workers upon the shorter, more direct methods of production, even though it has become unprofitable to employ them upon the longer, more indirect processes. Employment—although, be it noted, employment of a different kind to that which existed in the boom—begins to revive.<sup>1</sup>

What now has happened to the rate of saving? In the midst of the crisis it will probably have fallen very low. Even now in the first stages of recovery it cannot be high. Yet, as we know, unless the whole appalling business is to be gone through again, the rate of investment must be kept down to this point. This will mean that the recovery will be slow indeed—unless some steps

<sup>1</sup> But as we shall see in the next chapter, Dr. Hayek does not think that this is any solution. He believes that it is absolutely essential to increase the relative size of the producers' goods department if any substantial revival is to be achieved. He thinks that this must not be done by injecting new money into that department, but by taking money from the consumers' goods department and giving it to the producers' goods department. He does not object to the purpose of an inflationary movement but only to its method.

are taken to hurry it. We are back at the same point in the cycle at which we began. Will it not seem the elementary duty of the financial authorities to speed up the recovery by issuing credits to the makers of producers' goods—even if that does entail, in view of the insufficiency of savings—an increase in the amount of money in circulation ? The financial authorities, laments Dr. Hayek, will not hesitate to provide the new credits, and thus our feet will be planted once again upon the path that leads to the next boom, and the next crisis.

We shall offer a critique of this analysis in the next two chapters. But we must hasten to assure the reader that the feeling of dissatisfaction which he is no doubt experiencing is perfectly justified. The reader is, no doubt, objecting that, although Dr. Hayek's analysis is unquestionably both elegant and illuminating, it does not seem to be a *sufficient* explanation of those world-shaking phenomena which we call capitalist crises. What Dr. Hayek says may be true, we feel, and no doubt it explains much ; but is it, somehow, a sufficiently *substantial* theory to account for capitalist crises ? Dr. Hayek's theory is, after all, exclusively a theory of disproportions. It is an explanation of how disproportions between the size of the two departments of production, in relation to the demand for their characteristic products, arise. There is no doubt that such disproportions do periodically exist, and it is not difficult to agree with Dr. Hayek that they arise because money, the circulating medium, instead of passively mediating the exchange of commodities, is made to assume an active rôle, and so to falsify the true nature of demand.

But can we possibly believe that capitalist crises *consist* in such disproportions ? Surely there is much more to them than that. The phase of the cycle which we call a depression, and in which there are quantities of unemployed factors of production in both departments, has been, in the case of recent cycles, so long that we feel the utmost difficulty in supposing that it can be the result, merely, of delays in the re-allotment of factors between the departments, so as to make possible a response to the true demands of the consumers.

Surely the observed phenomena point insistently to there being some sheer quantitative factor at work ? Surely it is not

only, and not principally, that the productive system has got out of alignment with the pull of demand? Surely the pull of demand is to-day, for some reason, quantitatively inadequate<sup>1</sup> to make the system work at anything like full steam? The facts of the case make it almost impossible not to guess that there is to-day some progressive failure in the whole motive power, whatever it is, which makes the system work. There is an unmistakable feeling of the machine beginning to run down. Truly it is not running down evenly. It goes comparatively well for a time: then it stops with a jerk, then gets going again—only to be pulled up once more. Dr. Hayek seems to have explained adequately the stops and starts of this process. He has explained why the crisis of the system takes on an oscillatory form. But we cannot feel that he has accounted for the existence of the crisis itself.

In particular Dr. Hayek has given us no hint as to why the temptation to inject new money into the system should now be so strong. It will not do for him to say that this temptation is strong because it provides a short cut out of depressions. But why is the system depressed? If he answers, because the last depression was got out of in this illegitimate way, then we must go back through each cycle which the system has experienced. And we shall find that Dr. Hayek himself asserts that the disastrous expedient of inflation was not adopted to anything like its present extent a hundred years ago.

Dr. Hayek has clearly shown the pernicious character of the inflationary drug. He has shown us exactly how it injures the patient's constitution, but he has not shown us why the patient is evidently becoming more and more in need of this drug. There must be some vital element in the situation which Dr. Hayek ignores.

#### SUMMARY OF CHAPTER V

Importance of the conclusion as to the necessity of ever increasing doses of new money. A quantitative illustration. The

<sup>1</sup> As Professor Robbins put it in the passage which we cited in Chapter I, there are "discrepancies between total supply and total demand," which need explanation.

proportionate amount of money in each department all important. The absolute amount meaningless. How the last state of an inflation is always worse than the first. Necessity for a rapid growth in the size of the doses of new money. Crisis inevitable the minute this ever accelerating dosage stops. But why should it ever stop? Why not a perpetual boom? Why not a "high inflation"? Money ceases to function if the price-level rises fast enough. Why not stop when all factors are employed? Inevitability of crisis whenever you stop. The sudden shift of demand from the producers' to the consumers' goods department. The wind of demand and the ship of production. Inevitability of a jib. Dr. Hayek's analysis seen as a description of what would happen if the bankers did not flinch, rather than as a description of what does happen. In practice the bankers flinch. Hawtrey, Keynes analysis too monetary. Merit of Dr. Hayek's is to have shown the real, as opposed to the monetary, limiting factors. Dr. Hayek's definition of crisis: "a transition to less capitalistic methods of production": a reconstruction of the structure of production on a broader base. The beginning of the next cycle. Insufficiency of Dr. Hayek's analysis. Absence of any quantitative factor. Capitalist crisis not merely a delayed readjustment to a changed pull of demand. Dr. Hayek accounts for the oscillations of the crises, but not for the crises themselves.

## CHAPTER VI

### *Two Ways of Restoring Profits*

IN the last chapter we noticed that Dr. Hayek considered that the inflationary error of establishing a rate of investment in excess of savings was inevitable. Nor does he merely mean that he despairs of the emergence of bankers and politicians who can understand, and will act upon, his views. The only way, it will be recalled, in which the bankers could keep the rate of investment down to the rate of saving would be to push their interest rate up to the "natural" or "equilibrium" rate—the rate of interest, that is to say, at which they do not have to create any new money in order to meet the demand for loans. For at this rate of interest the current savings of the public satisfy this demand in full.

Now the only way in which the bankers can tell whether they are keeping the rate of investment down to the rate of saving is by noticing whether or not the total effective circulation of money is increasing. Hence this conception, namely "the total circulation," or "the total quantity" of money, is an extremely important one. We shall, then, be disappointed to find that it is a quite unascertainable quantity. In the last chapter of *Prices and Production* (in particular pp. 90–108), Dr. Hayek makes it clear that the bankers can never hope to control the quantity of money; for they can never know what that quantity is, nor even, with certainty, whether it is increasing or decreasing. In the first place (as we have noticed above), Dr. Hayek defines money extremely widely. He means by money cash, bank deposits, and commercial credits of every kind—in fact, "everything which serves as money, even if it does so only temporarily."<sup>1</sup>

<sup>1</sup> Dr. Hayek also introduces an argument which shows that "the quantity of money" depends for practical purposes on a somewhat complex conception which he calls "the co-efficient of money transactions." We need only notice that what is in question is the amount of money needed by a community to move a given quantity of goods through the various stages of production. This quantity depends upon the number of times such goods change hands during their transformation from basic raw materials to finished products. It depends, in other words, on the combination or splitting up of firms. We saw in Chapter II how vitally this question of how much buying and selling there was *within* the process of production affected monetary questions. For a neglect of this process was one of Major Douglas' errors.



Again, the quantity of money must always be understood in relation to the velocity of its circulation. In other words, a sudden increase in the velocity of circulation might, all unknown to the bankers, more than offset some decrease in the total quantity of all kinds of money which they had effected. No one who reads Dr. Hayek's argument will be inclined to question his conclusion that "the natural or equilibrium rate of interest . . . is incapable of ascertainment." We now feel the full force of the statement that the cardinal "mistake" of the bankers, in lending more than the public are saving, is inevitable. The bankers are working with incalculable quantities, nor do they at all fully control them. The best advice that Dr. Hayek can give them is always to stay on the safe side—"bankers need not be afraid to harm production by over-caution, even during times of general depression."

This conclusion is of considerable interest to us. We can now ask if Dr. Hayek believes that crises are an unavoidable part of the capitalist system or not. His answer, I take it, would be that, because of the complications introduced by the necessity of using money and credit, they are and always must be. He would not mean merely that crises were made inevitable by the fallibility of the human agents who work the system. He would mean rather that the existence of money and credit, of a medium of exchange, itself an indispensable feature of capitalism, introduces unavoidable instabilities into the system.

Dr. Hayek points out (p. 110) that equilibrium theory is, tacitly, based on the assumption of barter. It is the task of monetary theory "to cover a second time the whole field" and to show us "what changes in the conclusions of pure theory are made necessary by the introduction of indirect exchange." He has shown conclusively that the idea of many capitalist economists, that if the price level was kept constant the possibility of money producing instability would be eliminated, is a somewhat elementary illusion. He himself believes, it is true, that there is in pure theory a possibility of eliminating the disturbing influence of money. That possibility would be to keep the circulation of money of all kinds fixed permanently at a particular amount. His own analysis of the concept of the total of money in circulation has shown how remote this possibility is. It could

only be attained if omniscient and omnipotent bankers were able to offset exactly all changes in velocity, and in the co-efficient of money transactions, by equal and opposite contractions and expansions of credit. And yet this fixed circulation of money could alone produce what Dr. Hayek calls a "neutral money"—a money, that is to say, which mediated the exchange of commodities perfectly and passively, exerting no influence of its own whatsoever.

We catch here a glimpse of the idea that money is an indispensable, but mystifying, cloak which conceals the relationships of the innumerable buyers, sellers, producers and wage workers of the system. Its use, though even the simplest capitalist economy is unthinkable without it, is evidently one of the things which make it impossible to keep the system in equilibrium.<sup>1</sup>

The fact that Dr. Hayek regards the original sin of over-lending as fatal and inevitable does not, however, make it impossible to consider the question of what the nature of capitalism would be if it *were* possible to avoid this crucial error. Once this question is raised we can see that it follows logically from Dr. Hayek's whole case that such a capitalism would not know crises. It would be stable; it would be in permanent equilibrium; it would be the capitalism described in the treatises of the equilibrium economists. For, after all, Dr. Hayek is an orthodox equilibrium economist, who accepts all the fundamental concepts and categories of this school. He has merely specialized in the uncomfortably detached "special subject" of monetary theory and crisis analysis. And his conclusion is that equilibrium theory is perfectly sound but that things do not work out that way because it is impossible to prevent the medium of exchange from distorting and concealing the real nature of demand. If only the rate of interest could always be kept equal to the rate of saving and the volume and velocity of all kinds of money be kept fixed at an invariable figure, capitalism would be stable and no such things as the trade cycle or crises would occur.

Now this is a remarkable conclusion. Dr. Hayek believes that the condition of capitalist equilibrium is equality in the rate of saving and investment, *with a permanently fixed supply of*

<sup>1</sup> The nature of money is elucidated in Chapter XIX.

*money.* At first sight this conclusion will seem to the reader, as it seemed to most capitalist economists when Dr. Hayek first enunciated it, to involve a preposterously deflationary demand.<sup>1</sup> It means that if the total amount of money of all kinds in existence in the capitalist world adds up to-day to, say, £x million, it should never, no matter how gigantic an increase in production there may be, be allowed to increase by a single pound. Nay more, it means that if, during a period of trade recovery, the velocity of circulation should increase by, say, 25 per cent, an actual curtailment in the supply of money exactly sufficient to offset this increase in velocity should be made by the banks. No wonder an alarmed colleague called the Hayekian School "sadistic deflationists." All the same, unless Dr. Hayek's reasoning can be upset, this conclusion must follow.

What an extraordinary situation would result, then, from the adoption of Dr. Hayek's specific ! Just so soon as any signs of brisker trade appeared, the bankers, in order to restrict investment to the level of saving, would nip the recovery in the bud by raising their interest rates and so curtailing credit. Are not Dr. Hayek's critics fully justified in saying that if his advice were adopted capitalism would be reduced to a permanent state of economic prostration from which all recovery would be impossible ? "It may be true," his critics might complain, "that Dr. Hayek's policy would eliminate crises. But it would only do so by eliminating all possibility of recovery as well. Dr. Hayek would prevent the periodic collapse of the system, but only by keeping it permanently on its back." Has Dr. Hayek any answer to this pertinent criticism ? I think that he has ; but it is an answer which, for comprehensible reasons, he does not enunciate with all his accustomed vigour. Dr. Hayek is in favour of his extremely deflationary,<sup>2</sup> anti-expansionist policy in order to

<sup>1</sup> In fact, it seems to have rather taken its own author's breath away. For this is how it is first formulated in *Prices and Production* (p. 91): "Prima facie, I suggest that we should expect rather that, to be neutral in this sense, the supply of money should be invariable. The question is, can this be true ?" The reader who is feeling the complications which the questions of foreign exchange between "open" capitalist communities, and of different kinds of money, would introduce, should consult the next few pages of *Prices and Production*. Dr. Hayek successfully eliminates these questions as unessential to the point at issue.

<sup>2</sup> I am here using the term "deflationary" in a popular sense. Dr. Hayek would, I take it, repudiate the allegation of being a deflationist at all. He would define deflation as a net curtailment of the effective volume and velocity of

prevent the rate of investment from rising above the rate of saving. But is there not another device, besides the curtailment of investment, by which these two rates may be kept together? Of course there is. There is the expedient of raising the rate of saving.

How, then, can the rate of genuine, voluntary saving be increased in a capitalist society? Here is a key question. For, if the bankers must not effect recovery by means of a direct increase of investment financed by supplies of new, cheap money, the only chance of getting recovery at all is to stimulate voluntary savings to the maximum possible extent. For then, when these savings have been made, investment becomes legitimate.

Now there is only one effective method of stimulating saving. And that is to increase to the utmost possible extent existing inequalities in the distribution of wealth. We saw in Chapter III that Mr. Hobson's desire to minimize savings led him to advocate the redistribution of income from the rich to the poor. In exactly the same way, Dr. Hayek's desire to maximize savings leads him to advocate the redistribution of income from the poor to the rich. For the rich, and especially the very rich, save an incomparably higher proportion of their incomes than do the poor.

Thus we see that Dr. Hayek's proposal for avoiding inflationary over-lending and yet achieving a sufficiently high rate of investment to lift the system, steadily if very gradually, out of slump is to maximize the rate of saving. But this can only be done by allowing the accumulations of the rich to pile up in their hands: by refraining from taxing them and distributing the proceeds to the poor. Moreover, this will not in itself be enough. It will be essential not only to keep all accumulations intact, but also to allow them to pile up at the maximum possible rate. It will be necessary, in other words, so to arrange matters that the rent, interest, and profits of the rich should be as large as possible. And there is only one way of doing that; and it is to keep, not only social services, but also and above all wages, as low as possible.

It is important to realize the urgency of carrying through money, so that money ceased to be "neutral." And, of course, he is as much opposed to this as he is to net additions to the supply of money.

such measures with the utmost rigour if Dr. Hayek's policy is to have a chance of success. For, remember, he must rely wholly and solely upon the growth of voluntary savings in order to lift the system out of a state of prostration. Unless an ample and therefore cheap supply of money for investment can thus be provided from savings he must pursue an ultra deflationary financial policy; he must abandon "cheap money," raise his interest rates, and so begin to restrict his loans, just so soon as there appear even the first and faintest signs of a brisker exchange of goods. Everyone in the world except himself and his disciples will say that by so doing he will destroy every chance of recovery. Hence he must do everything else in his power to increase saving and hence "legitimate" investment. He must, at all costs, make it possible for the rich to save. For only so will he have the money to use for investment. And he can only achieve this by reducing taxation on the rich and by increasing their incomes in every conceivable way.<sup>1</sup> But what in plain English does increasing the incomes of the rich mean? It means increasing profits; it means making production profitable once again.<sup>2</sup> Hence it is clear that Dr. Hayek's positive policy for recovery is a restoration of the rate of profit. And in order to effect that object he makes the straightforward recommendation of cutting down wages and social services.

Dr. Hayek's policy, then, boils down to a particular way of making industry profitable again. But what about the opposite "expansionist" or "inflationary" policy advocated by the various schools of under-consumptionists? Dr. Hayek directs his formidable polemic against Professor Fisher, Mr. Hobson,

<sup>1</sup> If the reader will turn to the last page of *Prices and Production*, he will find that Dr. Hayek ascribes prolonged economic stagnation to such things as the existence of social services financed by redistributory taxation. Nor have his adherents (such as Professor Robbins) been slow to point out that the "worst" feature of such social services (of a "dole," in particular, of course) is that they maintain wage rates above the equilibrium or "natural" rate.

<sup>2</sup> For the various subdivisions into which we divide the incomes of the rich such as rent, interest, or even the high salaries and fees of the professional men who minister to the rich, depend in the last resort upon production itself being profitable. For example (as the American landlords have found to their cost), the landlords cannot get their rent unless it pays the farmers to farm the land. The eminent specialist cannot get his 500 guinea fee unless the eminent industrialist on whom he operates has been able to make a profit on his business. The retired gentleman at Cheltenham (as he, too, found in 1931-2) cannot draw his interest on his railway first preference shares unless that interest has been earned by the profitable operation of the railways.

and the weaker brethren amongst the capitalist economists, because they do not advocate the severe path of wage cutting. They advocate (for the most part) a raising of the price-level (by the injection of new money) to a point at which it stood in some former year and then its permanent stabilization at this point. But, as we have seen, in modern conditions of perpetual technical progress, and so perpetually falling costs, this amounts to a rapid and ever increasing restoration of profits. For profits *are* the difference between prices and costs. So that if prices are first raised and then kept permanently stable, while costs perpetually fall, profits will grow larger and larger.

We reach, then, the remarkable conclusion that the "expansionist," or, as Dr. Hayek would stigmatize it, "inflationary," policy is, equally with his own, a policy designed for the restoration of the rate of profit. Moreover, the similarity of the two policies goes further than this. Not only are they both designed to restore the rate of profit. They both go about this task in the same way ; they both work on the assumption that the only way to restore the rate of profit is to cut down the purchasing power of individual consumers. Their sole difference is that Dr. Hayek proposes to do this by cutting wages and social services, while the inflationists propose to do it by raising prices.

We can now appreciate the point which we hinted at in the footnote on p. 78. Dr. Hayek does not object to an inflationary or expansionist policy because its initial effect is to reduce the relative purchasing power of individual consumers. Dr. Hayek is in full agreement as to the necessity of cutting down the real incomes of the vast majority of the population. His objection to the inflationary method is, precisely, that it fails to cut down individual purchasing power effectively or permanently. The new money, he complains, inevitably gets into the hands of the individual consumers after a short time.

It is important to grasp this point because Dr. Hayek's analysis sounds as if it might lead up to the conclusion that all would be well if the attempt to cut down individual consumers' purchasing power were *not* made. As we put it in the last chapter, he considers that crises occur because the injection of new money falsifies the true direction of demand by making it appear that people are saving more and spending less than they are doing.

Does Dr. Hayek consider, then, that the solution is to obey the actual pull of demand, to allow the consumers' goods department to grow, or, at any rate, to maintain its size relatively to the producers' goods department? Nothing could be further from his thoughts. He is in perfect agreement with the inflationists as to the necessity of cutting down the relative size of consumers' demand, if there is to be any revival. His complaint is that the inflationary method only appears to effect this purpose, or, at any rate, only effects it temporarily and precariously. His own policy of directly taking money from the individual consumers and lending this money to the producers of producers' goods is designed to effect exactly the same purpose, but to effect it permanently and securely. Hence both the inflationary policy and Dr. Hayek's so-called deflationary policy have exactly the same objective, namely, the reduction of the demand of the individual consumers. Moreover, we can now see what the object of this apparently eccentric policy is. All the capitalist economists wish to cut down the individual consumers' purchasing power because only so can they restore the rate of profit.

We seem to have stumbled across, almost by chance, and after much argument, a concept that would, one might have thought, have been very useful to us in the first place: the concept of the rate of profit. It certainly seems that raising the rate of profit would be much the simplest way of defining the object of both the price raising policy advocated by the inflationists and of the wage cutting policy advocated (a little coyly) by Dr. Hayek. It may, of course, be true, as Dr. Hayek insists, that his is the only sound way of restoring the rate of profit (or rather that it would be if it were possible fully to adopt it, which he agrees it is not). *The fact remains that we have discovered that both his own policy and the policy which he abominates have the same object: namely, the restoration of the rate of profit.* Is it not strange that in all the voluminous literature devoted to the question this fact is never stressed? It is, it seems, always tacitly assumed.<sup>1</sup> And yet a clear realization that it is common ground between all the disputants that a restoration of the rate

<sup>1</sup> Some capitalist economists do define the crisis as a fall in profits. Thus Professor Robbins writes: "One way of describing the slump was to depict it as a simultaneous break-down of the profitability of many different lines of industry." (*The Great Depression*, p. 30.)

of profit, by this method or that, by the "fair" means of wage cuts and voluntary savings, or the "foul" means of credit expansion, is the one thing which can possibly bring recovery, is essential to any understanding of the problem.

For until we understand this, we do not know what the various schools of capitalist economists are quarrelling about. They are, it is true, quarrelling about how to bring recovery and how to bring it in such a way as to avoid the recurrence of crises. *More precisely, however, they are quarrelling about how to restore the rate of profit.* And necessarily so. For they are all tacitly agreed, and they are quite right, that the only way in which recovery can come to capitalism is to make the operation of existing plants, and consequently the building of new plants, profitable again. The simple, essential fact that old plants cannot be operated, nor new plants built, unless it is profitable to operate and build them, is at the heart of the question of "recovery." It means that the obvious pre-condition of recovery—too obvious apparently to be mentioned by most writers on the subject—is to restore the rate of profit in industry at any rate to the minimum figure which will make the wheels go round again. And the whole quarrel between Dr. Hayek and the other capitalist economists, such as Professor Fisher, is really about which way this restoration of the rate of profit is to be effected.

For clearly there are two ways in which you can make production profitable again. You can lower costs or you can increase prices. And both ways involve reducing the purchasing power of the population at large. The less responsible capitalist economists<sup>1</sup> think it should be done by raising and then maintaining prices. Dr. Hayek thinks that it should be done entirely by lowering costs. This is really the extent of the difference between them.

But this agreement on aim is obscured by the fact that in modern conditions, owing to continual technical progress, costs are coming down all the time—of themselves as it were. Hence

<sup>1</sup> In the earlier half of the nineteenth century predominant economic opinion would have agreed with Dr. Hayek, and he looks back regretfully to that more enlightened age. See *Prices and Production*, p. 100, where Dr. Hayek quotes John Fullerton to show that in the 'thirties and 'forties of the last century majority opinion in the British Parliament regarded the demand for a net addition to the supply of money as in all circumstances illegitimate. Such was the vigour of capitalism's youth!



the ordinary "unsound" way of restoring profits need not consist in raising prices: it will be sufficient to expand credit enough to prevent prices falling as costs fall. Similarly, Dr. Hayek's "sound" way consists, not merely in eschewing an increase in prices, but in cutting costs so rapidly that profits appear, even though prices continue to fall. This is the great confusing factor in the modern situation which has deceived so many economists, both professional and amateur. The now perpetual fall in costs of production makes the whole economic situation dynamic instead of static. It is as if the very landscape about which we are trying to find our way was itself moving. Hence it may be necessary to move at a certain speed in a certain direction even to stay where we are! All our movements must be calculated in relation to the movement of the landscape itself. It reminds one of the Red Queen's remark to Alice—"Here, you see, it takes all the running you can do to keep in the same place. If you want to get somewhere else you must run at least twice as fast as that." In the same severe spirit Dr. Hayek tells the capitalists that, if they mean to restore the rate of profit without inflation, they must not only cut costs by means of technical improvements as fast as prices fall, but that they must also cut wage costs in order to get ahead of the fall in prices.

For the fall in costs, due to technical improvements, will merely balance the fall in prices which (as we have seen) must also take place, if money is not expanded. This might be all right in a period of existing prosperity. Profits, it might be supposed, would in these circumstances remain the same. But this would not be enough to lift the system out of slump. In order to do that it is necessary to increase profits. And for this purpose wage rates must be cut so that costs may fall faster than prices. Reductions in costs effected by technical improvements will, to return to our analogy, enable capitalism to run fast enough to stay where it is. But, in order to get anywhere, in order to get to prosperity out of a depression, for instance, it must mend its pace by cutting wages as well.<sup>1</sup>

Our discovery of the identity of aim between the policies of

<sup>1</sup> This consideration lets us catch sight of the idea that there may be a difference between reductions in costs effected by technical improvements and reductions in wage costs. For cannot a reduction in cost effected by technical improvement be expressed, in the last analysis, as the production of a given output with

Dr. Hayek and his opponents should not make us conclude, however, that there are not real and important differences between his and their alternative ways of restoring the rate of profit. It will be convenient if we summarize these differences here.

The reader will probably agree that Dr. Hayek makes out a powerful case for supposing that the use of the credit expansion, price raising or maintaining, method has had much to do with the violent oscillations of the system. Nor does the fact that he admits that his is a counsel of perfection destroy the practical importance of his conclusions. For it is obvious that in practice it is not a question of *which* way you choose for restoring the rate of profit. In most instances both methods are sure to be resorted to. In every acute depression the financial authorities will try to restore profits by bolstering prices by means of a policy of cheap money and liberal lending. But at the same time the capitalists will try to restore profits by cutting wages and social services. Hence the practical point is the question of the extent to which each method is resorted to. According to Dr. Hayek's analysis, it is clear that, in so far as the rate of profit is restored by cutting wage costs, and consequently the recovery is effected by real savings, the recovery will be "sound"—*i.e.*, it will be permanent, it will not contain the seeds of its own destruction. Similarly, in so far as the rate of profit is restored by price raising or maintaining, and new investments are financed by new money, the volume of new savings failing to rise sufficiently to cover them, the recovery will be "unsound,"—*i.e.*, it will be transitory and will lead directly to a new crash.

This consideration enables us to appreciate the full horror with which the Hayekian school regards the American New Deal and the whole financial policy of the present American Administration. For there can be little doubt that, on Dr. Hayek's arguments, of all the expedients that have ever been employed to bring back recovery after a capitalist crisis, the devices now being employed in the United States are the least sound ; are the most certain, that is to say, to produce new and unparalleled catastrophes.

fewer workers, and so a lower net wages bill, but with the same wage rates ? And cannot a reduction in costs due to a cut in wage rates be expressed as the production of a given output with the same number of workers, but with each worker paid less per unit of output ?

The American authorities are relying almost wholly upon a policy designed to raise prices and are hardly even attempting to cut wage costs. (Indeed, they have made a show of increasing them.) Their main expedient is direct monetary expansion. They are "injecting new money" into the American capitalist system by means of creating credits for producers upon a scale never yet dreamt of. The Agricultural Adjustment Administration and the Reconstruction Finance Corporation are, in fact, institutions designed for this special purpose. They make loans at low rates of interest to farmers or industrial producers who are in difficulties. And why are these gentlemen in difficulties? Because, Dr. Hayek would sternly remark, they have not sufficiently cut their wage costs. Hence the main effect of the accommodation which they are receiving is to enable them to avoid cutting wages—to enable them to raise their selling prices instead.

The result has been a steady rise in the American price-level. The American price-level has risen more than have money rates of wages. The money wage increases have been more than balanced. Hence the whole of the drop in "technical costs" which has taken place since 1929 has gone to profits. The rate of profit for the great corporations has been considerably restored in the year and a half that has passed since March 1933. But it has been restored almost entirely by the injection of new money.

The essential character of the New Deal as a determined effort to restore the profitability of the American productive system by the inflationary method has been enormously obscured, however, by the welter of political expedients by which this purpose has been effected. Hence the confusions into which not only the New Deal itself, but its critics also, have fallen. Professor Robbins, for example, has not grasped the realities of the contemporary American situation. He writes :

"It is as yet too early to say whether the American emergency legislation will prevent the coming of some degree of recovery. The various measures which have been introduced each work in such different directions. The National Recovery Act raises costs and fosters monopoly. The Agricultural

Adjustment Act restricts output and subsidizes immobility. The Gold Policy attempts to raise prices by a method which increases the scarcity of gold and imposes the maximum inconvenience on the world at large. The unbalancing of the budget and the vast expenditures on public works have an inflationary tendency which may well override the various impediments to enterprise created in other directions and engender an inflationary boom—which, if the analysis of earlier chapters is correct, would be likely to be followed by a deflationary collapse. It would be futile to attempt to assess in detail the relative importance of these various and rapidly changing influences.” (*The Great Depression*, p. 128.)

No one will deny the apparently conflicting nature of the successive moves of the American Administration. The American producers have been loaded with increased costs by reducing hours of work and imposing some wage minima. How, then, can we say that the object of the whole programme is to restore and increase profits? The answer is simple. With one hand the Administration increases costs, but with the other it increases prices. And the hand which increases prices always works faster than the hand which increases costs. Now profits, as we have seen, are the gap between costs and prices. Hence one way, though at first sight no doubt, an eccentric way, of increasing profits is to raise both costs and prices, but to raise prices more than costs. And this is the essence of the policy of the Roosevelt Administration.

Nor is there any difficulty in accounting for the fact that Mr. Roosevelt and his friends chose this peculiar and confusing way of restoring profits. It is usually politically impossible for capitalist governments, other than fascist dictatorships (and it is dangerous for them), to restore the rate of profit entirely by cutting wages, etc. It is sometimes politically impossible for a capitalist government to cut wage costs at all. It has to rely entirely upon a monetarily effected increase in prices, however unsound Dr. Hayek may show such a policy to be. But the Roosevelt Administration, in the peculiar circumstances in which it found itself, did not even dare to restore the rate of profit by leaving wage costs constant and increasing prices. As

a liberal, left, popular, democratic Administration it felt that it was incumbent upon it actually to increase wage costs. But if it increased wage costs and did nothing else, it would clearly produce not revival, but the complete cessation of all production. For the rate of profit, which was already very low, would be extinguished entirely. Hence if wage costs were to be increased, prices had obviously to be increased also; and they had to be increased more than wage costs in order that profits might reappear on a scale sufficient to galvanize the system into renewed activity.

These circumstances account not only for the confusing nature of the New Deal, but also for its peculiar, and to some tastes nauseating, character of duplicity. Much is given with one hand, only it is all (and always a little more than all) taken away again by the other.

Now what must be Dr. Hayek's view of such a policy as this? Is it not clear that on his reasoning of all the unsound methods of securing revival the New Deal is far more unsound than any that have ever before been adopted by a capitalist government? Dr. Hayek considers that the only sound way of restoring economic activity is to do so wholly by means of cutting wage costs, to eschew "reflation," to use a characteristic American term, altogether. Most capitalist governments, in fact, get out of slumps by a mixture of wage cutting and credit expansion. Some, in particularly difficult situations, have resorted entirely to the unsound expedient of credit expansion and have left wages alone. But what is Dr. Hayek to say of the Roosevelt Administration? For Mr. Roosevelt raises money wages and then raises prices sufficiently to more than offset his own action. What will happen if there is even an element of truth in Dr. Hayek's theories? Is it not clear that some recovery will continue just so long as the expansion of credit, or, as Dr. Hayek would call it, the injection of new money, is continued—and continued in ever more massive doses? As soon as this ever more rapid inflation is stopped (and we have seen the reasons why, sooner or later, it must be stopped), the rate of investment will collapse, and the New Deal will become the New Collapse.

Now there is no doubt, as we shall demonstrate in subsequent

chapters, that the present policies of the American Administration constitute an almost perfect specific for renewed catastrophe. Can we, however, put as much weight as does Dr. Hayek upon the fact that the rate of profit is being restored by an inflationary boosting of the price-level instead of by a process cutting wage costs? Can it be true that, while the inflationary method being used is certain to produce catastrophe, Dr. Hayek's method of wage cutting would produce permanently stable prosperity? Let us recall his distinction between the effects of the two methods of restoring profits. The nemesis of the inflationary method was that as the new credits percolated through from the producers' goods department to the individual consumers, a counter-pull from the consumers' goods department was set up which, unless it was counteracted by ever new and larger credits, drained the producers' goods department of non-specific factors, and in general set up a type of demand to which the system was unable to respond. The merit of the wage cutting method was that the additional money given to the producers' goods department had been saved, had been given up, that is to say, by the individual consumers. Hence there was an initial drop in the money demand of the consumers' goods department and when, therefore, this money percolated back again to the consumers' goods department it merely restored the old level of consumers' money demand. There was no net increase in consumers' money demand.

This is a real distinction. There is good reason to suppose that if a revival could be financed entirely by voluntary savings, produced by such vigorous wage cutting that industry became profitable again in spite of a continual fall in prices, it would be a more stable revival in the sense that it would be more gradual and of longer duration, than are revivals produced by inflation. But can we possibly believe that the difference between the two methods of restoring the rate of profit is so great that the one will produce dire catastrophe and the other the hitherto unsighted goal of permanent capitalist stability?

After all, the difference between the two methods is wholly monetary. They are, if you think of it, two different ways of cutting down the effective purchasing power of individual

consumers (predominantly wage earners, of course).<sup>1</sup> The inflationary method does this by raising (or preventing the fall of) the price-level and so making people's unchanged money incomes buy less than they would have done. The Hayekian wage cutting method does the same thing by the more simple and direct route of taking some of their money away. It may well be that this method would lead, if it could be adopted, to less confusion and instability than the other. For it depends less on the mystifications of money and credit. The wage earner is openly instead of secretly robbed, and he does not have the subsequent opportunity to struggle to improve his standard of life which is given him by the inflationary method. But can we put the difference between them any higher than that? Can we possibly suppose that the more open wage cutting method would result in permanent stability?

#### SUMMARY OF CHAPTER VI

Inevitability of inflation admitted by Dr. Hayek. The quantity of money unascertainable. Crises in practice inevitable, Dr. Hayek supposes, because of the mystifications of money: crises evitable in pure theory if the supply of money could be permanently fixed. Startling character of this conclusion. Supreme necessity to maximize saving in these circumstances. In order to maximize savings you must give more to the rich and take more from the poor. Urgent necessity for Dr. Hayek to cut wages and slash social services. *Dr. Hayek's practical policy defined as a restoration of the rate of profit.* But the under-consumptionists' policy also turned out to be a policy for the restoration of the rate of profit.

Identity of aim between Dr. Hayek and his opponents. The

<sup>1</sup> Let the reader get the full implications of this remark. It is the case that all capitalist methods of obtaining recovery turn out to consist in *diminishing* the amount of the community's purchasing power for consumers' goods: for only so can the production of producers' goods be made profitable. For the purchasing power taken from the individual consumers is used to create a demand for producers' goods. But, the reader will at once object, how can the production of producers' goods, the only object of which must ultimately be to produce new consumers' goods, be made permanently profitable by the contraction of the market for consumers' goods? This common-sense objection, we shall find, strikes at the very roots of the present difficulties of capitalism.

quarrel turns out to be merely on the question of method. Under-consumptionists want to raise prices. Dr. Hayek wants to cut wages. This remarkable fact obscured, however, by the nature of the contemporary situation. Costs falling rapidly and constantly to-day owing to technical progress. Hence the landscape itself is moving. Dynamic character of the present economic situation. Dr. Hayek compared to the Red Queen. Difference between Dr. Hayek's and the under-consumptionists' method of restoring profits defined.

Application of Dr. Hayek's reasoning to the American New Deal. Mr. Roosevelt confuses Professor Robbins. Real character of the New Deal as a determined effort to restore the rate of profit of American industry not in doubt. Mr. Roosevelt's method to raise both prices and costs, but always to raise prices more than costs. Apparent eccentricity of this method explained by the exigencies of the President's political situation. Explanation of the duplicity of the New Deal. Catastrophic unsoundness of the New Deal according to Dr. Hayek's argument. Limits, however, to the difference between restoring profits by his method and by the expansionist method. Main difference is on the question of whether the great majority of the population shall be openly robbed by cutting wages or covertly robbed by raising prices.



## CHAPTER VII

### *The Dilemma of Profits or Plenty*

THE last four chapters have been devoted to a comparison of the two main lines of policy advocated by capitalist economists for the cure and prevention of crises. We contrasted the inflationary method of bolstering prices, advocated by such authorities as Professor Fisher and Mr. Hobson, with the deflationary method of cutting costs advocated by such authorities as Dr. Hayek, Professor Robbins and their disciples. Both methods are different ways, we found, of restoring the rate of profit. Both are based firmly, if tacitly, on the platitude that under our present system a restoration of the rate of profit is an absolute pre-requisite to recovery.

And yet this platitude, when looked at more closely, seems to contain a paradox. Let us compare again the expedients advocated by the two schools. The inflationary method issues new money, creates monopolies, organizes the wholesale destruction of already produced commodities, and "regulates," which means in practice reduces, the production of new commodities. The object of all these expedients is to raise prices. The Hayekian method cuts wages, cuts social services, and reduces taxation upon the capitalists. Its object is to reduce costs. Now these alternative expedients, namely raising prices or cutting costs, are both rational measures for the purpose of restoring the rate of profit. For, as we have seen, profits are the gap between prices and costs. But are they so obviously rational measures for the broader purpose of restoring prosperity? That all depends on what we mean by "prosperity." Now probably what most people mean by prosperity is a condition of things in which everybody can purchase an adequate supply of commodities. Is then the cutting down of everybody's purchasing power, *either* by raising prices *or* by cutting wages, a rational method of achieving prosperity in this sense?

There can be no doubt that profits are increased by high prices and low wages. Nor is there any doubt but that an increase in profits is the one thing which can stimulate the capitalist system into renewed activity. Therefore, say all schools of

capitalist economists (differing only as to method), if you want prosperity, raise prices and/or cut wages. But equally who can doubt but that high prices and low wages are *not* the way to enable the mass of consumers to obtain an adequate supply of commodities? On the contrary, it must be obvious that *low* prices and *high* wages are the one thing that will do that. But high wages mean high costs. For as we have begun to see costs and wages<sup>1</sup> appear to be the same sums of money looked at from the producers' and the consumers' point of view respectively. We have come to the inescapable conclusion that one policy will restore profits, while exactly the opposite policy will permit of an adequate supply of commodities to the population. It seems impossible to have it both ways. You can raise prices and cut costs, and thus restore profits. But if you do, you will tend to make it impossible for the public to obtain commodities. Yet if you cut prices and raise costs you destroy profits, and a moment ago we agreed that the only method by which you could make the wheels of capitalist production go round at all was to restore profits. Now we find that in restoring profits you will prevent consumption. To what strange paradoxes has our argument led us!

Yet they are not new paradoxes. Everyone must surely have noticed one remarkable feature about all the specifics for recovery which the capitalist economists and statesmen offer us. Either they tell us that all will be well, that the present glut of unsold goods will soon be disposed of, if only the money incomes of the mass of consumers are reduced (Dr. Hayek). Or they tell us that we shall all be able to buy the necessities which we now lack—if only the prices of these necessities can be sufficiently raised (Professor Fisher, Mr. Roosevelt, and a hundred others).

We seem to have reached an issue which goes deeper than any which we have so far discussed. At the end of the argument we have come upon the fact that there is an extraordinary

<sup>1</sup> "Wages," in the widest sense of the term, *i.e.* payments made to persons in respect of their services in the process of production. As we have already found, the concept "costs" is not so precise as it sounds. Are all costs labour costs in the last analysis? If so, this statement of the case needs no qualification. Or are there other costs? If so, of course, plenty for the consumer is helped, not hindered, by their reduction. We shall have much to say about this point later on. For the moment let it lie.

antinomy between profits and plenty. The measures which will maximize profits will minimize plenty : the measures which will maximise plenty will minimize profits.

Yet the essence of our present system is that production can only take place when it is profitable. Profit is alike the prime mover and the governor of the system. To expect the unfortunate capitalist system to work if the production and distribution of goods is not profitable is like expecting a motor-car to go without either petrol or a steering wheel. Yet it seems that the very measures which will restore profitability will destroy the possibility of plenty by drastically reducing the consumers' purchasing power. Nor, when we come to think of it, is this such a surprising discovery. The scarcity of a commodity, the capitalist economists have taught us, is what makes it possible to derive profit from its production or transportation. At any rate, some degree of scarcity is necessary. Demand does not seem to be able to do it alone. For the thing which human beings demand most imperatively is air. Yet no capitalist has yet found a way of deriving profit from the production of air. There is too much of it for that. Can we be altogether surprised, then, that just in so far as other commodities begin to approximate to the condition of air, begin to get plentiful, that is to say, it becomes harder to derive much profit from their production? Or, again, is it not natural that as capital becomes more plentiful it should command a lower rate of profit? For profit can be thought of as the hire of capital resources. As these resources become more and more plentiful the hire which they can command naturally tends to drop. Profit and plenty are evidently not good bedfellows.

This suggests to us that there may have been some element of truth after all in what the extreme credit crank theorists were trying to say. So far as most of them are concerned, this suggestion flatters them. In spite of their stress on the poverty in the midst of plenty paradox, they are even further from a grasp of the antinomy between profits and plenty than are the professionals. Major Douglas and his friends innocently suppose that the establishment of plenty, the furnishing, that is to say, of the population with the purchasing power necessary to obtain all the commodities which modern productive methods could

give them, is compatible with maintaining a system dependent upon profits for its motive force and its regulation. One American amateur economist, Mr. Stuart Chase, has, however, caught sight of the dilemma. His most recent book, *The Economy of Abundance*, is full of the problem. "Abundance," he writes, "is not alone a promise to mankind, it is a savage threat to the real or supposed interests of special and powerful groups of men everywhere. . . . Gain was at a maximum when the commodity was scarce."

Mr. Chase goes on to make a sharp distinction between what he calls "vendibility" and "serviceability." He points out that commodities are produced not for "serviceability"—for use, that is to say—but for "vendibility." By "vendibility" he means for the sake of the money against which they may be exchanged. And this money must be sufficient, he points out, to cover costs plus profit. Hence to say that goods are produced for vendibility is only another way of saying that they are produced for profit. There is no doubt that Mr. Chase has caught sight of the difficulty. Disappointingly enough, however, this has not prevented him from retaining most of the more elementary illusions of the credit cranks. When he comes to his remedial proposals he can only suggest that we should distribute more money to the mass of consumers. He blandly implies that it would be possible to retain the central feature of the present economic system, *viz.*, the private ownership of the means of production, and yet to destroy its one motivating and regulating force of profit.

Thus in the end we have to admit of Mr. Chase, as of all the other amateur capitalist economists, that his service is confined to pointing out the existence of the problem. This failure to arrive at any kind of solution is inevitable since none of these writers have ever clearly realized what it is that they are out to achieve. Are they out, like all professional capitalist economists, and all capitalist politicians, to restore activity to the present system by making it once again profitable to produce goods and to employ men? Or are they out to achieve the maximum possible distribution of commodities to the whole population? If they are out for the first objective, they will take almost exactly opposite measures to those indicated for the achievement of the

second. Unfortunately, however, they have never decided which of these things they are out to do. Indeed, with the partial exception of Mr. Chase, they have not even realized that there was any choice. They have hopefully assumed that anything which will create plenty will also create profits. They have lumped plenty and profits together under loose general terms such as "recovery" or "prosperity." Hence the peculiar confusions into which they fall.

Mr. Chase's glimpse of the fact that an opposite policy will restore profits to that which would create plenty<sup>1</sup> caused him to make the following comment on the New Deal:

"The Roosevelt Administration (Feb. 1934) cannot make up its mind whether it wants to restore vendibility—popularly known as Recovery—or inaugurate a new economic system based on serviceability. Obviously, until this choice is made, the conflict will be reflected in zig-zag administrative performance" (*op. cit.*).

Mr. Chase imputes his own indecisions to President Roosevelt. President Roosevelt and his advisers labour under no such divided counsels. Their object is to restore profits, and they are, partially, achieving that object with vigour and ruthlessness, albeit in a manner which Dr. Hayek and his school can show to be peculiarly disastrous to the stability of the system. President Roosevelt has made it categorically clear that he stands by what he calls a "fair profit" in industry. And the whole balance of his policy is to restore such profits.

We find that there is an unseen confusion at the bottom of the controversy between the amateur and the professional economists of capitalism. What the professionals are able to prove is that the remedies of the amateurs would not produce the plenty which their authors promise. For, under capitalism, a pre-requisite, not merely of plenty, but of any supply of commodities at all, is the existence of a sufficient rate of profit to make it worth the while of the owners of the instruments of

<sup>1</sup> Would create plenty, that is to say, if capitalist production could be carried on at all without profits. Actually the policy of Mr. Chase, Major Douglas, or any other of the credit cranks, if we can conceive of it being carried out at all, would stop all production. For it would abolish profits. Plenty, therefore, can only be created after the expropriation of the means of production and the organization of production for use. For only then can we dispense with profits.

production to keep them in operation. But any such policies as Social Credit which, if they could be put into operation at all, would create plenty, would reduce profits to below this point. Just in so far as they did begin to produce plenty they would defeat themselves and stop the wheels of industry from turning at all. A direct attempt to produce plenty without a change in the ownership of the means of production wrecks itself at once, since it takes no account of the fact that plenty will destroy profits, and that profits, so long as the means of production are privately owned, are a necessary condition for any production at all.

This explains why the professional economists say that the way to recovery is to create scarcity, by cutting down people's incomes, in order to increase profits, and so by this roundabout way to stimulate production. At length, however, the amateurs, in the person of Mr. Chase, at any rate, are beginning to have their revenge. They are beginning to be able to show what a strange expedient is the creation of artificial scarcity as the first step towards plenty. And Mr. Chase has succeeded in linking this extraordinary hankering for scarcity with the need to revive profits.

In the end, then, we must feel that each school has a good deal of success in refuting the other. The professionals are able to show conclusively that the effect of such policies as Social Credit would be, not plenty for everyone, but a complete arrest of all production for lack of profits. The amateurs are able to indicate that what the professionals' remedies will produce is certainly not plenty : they may produce renewed profits and so renewed industrial activity. But they can do so only at the cost of artificially creating and maintaining a state of scarcity for the overwhelming majority of the population.

This tangle of confusion has arisen from a failure to define what is meant by such terms as "recovery" or "prosperity." The professional economists, we now realize, mean by these terms a restoration of the rate of profit. (There is, we have seen, an internecine quarrel amongst them as to whether this should be done by creating scarcity by means of raising prices or by cutting costs. But this does not at the moment concern us.) The amateur, social credit cranks mean by "recovery" and "prosperity" a plentiful supply of commodities for the whole population. But they ignore the fact that, unless they change

the social system, the provision of any supply of commodities to anybody depends on the maintenance of an adequate rate of profit, and that their proposals flout this necessity.<sup>1</sup>

We must now ask whether the professional economists have not themselves considered this dilemma. Do not they, too, promise plenty in the end? Do they not claim that a restoration of the rate of profit is but a means to that end? Surely they must have some answer to the "plain man's" point that reducing purchasing power by cutting wages and/or raising prices seems a funny way of getting rid of our now chronic glut of commodities.<sup>2</sup>

They have such an answer. The most responsible capitalist economists would, if I understand them aright, reply somewhat as follows. It may seem paradoxical that it is necessary to start the process of recovery by cutting down people's purchasing power. None the less, this is the case. For this is the only way by which profitability can be restored to industry. "If profitability is to be restored, costs must be cut," writes Professor Robbins (*The Great Depression*). (Or prices be raised, of course.) Indeed, some such apparently paradoxical policy as an initial reduction in consuming power, as the first step to recovery, is latent, when you come to think of it, in the whole analysis of the Hayek-Robbins school. This fact is revealed in a significant phrase of Professor Robbins. Professor Robbins writes: "One way of explaining the coming of the depression is to say that

<sup>1</sup> This, I think, is the paradox which worries Mr. E. F. M. Durbin, when he points out that Dr. Hayek's analysis takes no account of the fact that the demand for producers' goods is ultimately conditioned by the demand for consumers' goods. Dr. Hayek does ignore this fact. But in a sense, as we shall see, this is just the merit of his analysis from a capitalist standpoint. For the business of capitalism is not the provision of consumers' goods, but the building up of stocks of producers' goods. Therefore for capitalism the object of the creation of producers' goods (means of production) is not the provision of more consumers' goods. The creation, the accumulation, of means of production is for capitalism an end in itself. All the same, it is the insanity of this aim, in modern conditions, which brings capitalism into collision with its environment. But we anticipate the argument of Part IV.

<sup>2</sup> Is it not a frightful comment on the degree of mental stupefaction that capitalist education, Press, and propaganda can produce, when working at top pressure, that this question is not asked by the "plain man" a thousand times more insistently than it is? I recollect that the solemn dicta of British Conservative and Labour statesmen in 1931, that the only way to get rid of the unparalleled glut of commodities which then existed was to impose cuts on everybody's incomes, were seldom exposed as the self-evident nonsense that they were. What, of course, the said statesmen meant was that cuts were the only way to restore profits. And there they were right.

the demand at the consumers' end has become relatively too high " (*ibid.*, p. 70). From this it follows naturally enough that the way to recovery lies through a cutting down of demand at the consumers' end. Nor is there any difficulty in understanding that to cut down the consumers' demand, to cut wages, that is to say, is the way to restore profits. But how do Dr. Hayek and Professor Robbins meet the point that by thus restoring profits they will reduce still further the ultimate demand for consumers' goods?

Ah, they will say, you must observe that it is only the rate of money wages which must be reduced. The total wages paid out by the productive system will be actually increased. For the restoration of profits will have made it possible to employ all the workers again. The effect of the initial cut in wages will be to increase employment and so maintain, or even increase, total purchasing power, even though each individual wage earner in employment will get less.

But what will happen now? Now, at last, all will be well, our instructors tell us.<sup>1</sup> Money wages will remain constant, it is true. But real wages will now begin continually and without interruption to rise. The ever continuing reduction in technical costs will be operating all the time. Production will be growing, prices will be falling. Profits, however, will be maintained, since costs are dropping also and in proportion. The maintenance of profits will keep the productive system in full employment: the fall in prices will continually distribute the ever growing wealth to everybody. Money incomes will remain constant, but real incomes will continually rise. We shall have reached the Nirvana of permanent, though progressive, equilibrium. The initial sacrifice of the workers in accepting a reduction in wages: the "courage" of the authorities in committing themselves to the paradoxical policy of cutting wages in order to increase consumption, will have been rewarded a hundredfold.

It all sounds too good to be true. And so, alas, it is. A brief prolongation of the Hayek-Robbins line of reasoning beyond the point at which they, prudently, abandon it, will demonstrate this sad fact. We have said that technical improvement is

<sup>1</sup> On the assumption that the financial authorities could be prevented from inflating.



continually reducing costs. But how is it reducing costs? By enabling the employers to produce a given output with fewer workers, and, therefore, with a lower wages bill. That is what we mean by an improvement in technique. Hence, no sooner will full employment at the lower wages have been achieved than a counter tendency, a tendency to throw men out of employment again, will begin to make itself felt. How can this tendency be offset? We saw that the way in which men already unemployed could be got back into work again was to cut money wage rates. Is it not clear that the same line of reasoning will show that the way to prevent men being thrown out of work again is also to cut money wages?

We saw that in order to restore full employment costs had to be cut *faster* than prices fell—in order to raise the rate of profit. Money wages had to be cut, in other words, as prices and costs fell, in order to keep real wages constant. But now, when we have assumed that equilibrium (*i.e.*, full employment) has been reached, is it any longer necessary to keep real wages constant by cutting money wages? The rate of profit has already been restored. Surely, therefore, there is no need to increase it? And yet we have just seen that it looks as if it must be necessary to do something to prevent unemployment reappearing. Can it be that there is also an inherent tendency for the rate of profit to fall?

This raises an issue which we have not yet faced up to. We have talked a great deal about the need to restore the rate of profit. But how did that need arise? Surely it does not help us much to say that the rate of profit had dropped because of the crisis? We must, as the capitalist economists themselves insisted in their polemic against Mr. Hobson, account for the occurrence of crisis. We must start with full employment of the factors of production and show how a crisis occurs. Now a crisis is a sudden falling off in the profitability of the productive system. (This, we remember, is how Professor Robbins himself defines a crisis.) Thus it is clear that there must be something which has caused this critical falling off in profitability. It looks as if there must be some inherent tendency for profits as well as employment to fall. For we noticed that all the specifics of the rival schools of capitalist economists were in fact different ways of applying artificial

respiration to the rate of profit. This is strong evidence that there must be an inherent tendency for the rate of profit to drop.

We shall be interested to find, therefore, that Dr. Hayek himself agrees that there is such a tendency. He describes this tendency in a passage in *Prices and Production* which seems to have been widely overlooked. He defines both the necessity of profits if capitalist production is to be carried on and their disastrous tendency to disappear, as follows :

“ The total amount of money received for the product of any stage ” (of production) “ will regularly exceed the total paid out for all goods and services used in this stage of production. Yet that margins of this kind ” (*i.e.*, profits) “ must exist is obvious from the consideration that, if it were not so, there would exist no inducement to risk money by investing it in production rather than to let it remain idle. To investigate the relationship of these margins to the peculiar advantages of the roundabout methods of production would lead us too far into the problems of the general theory of interest. We must therefore be content to accept it as one of the definite conclusions of this theory that—other things remaining the same—these margins must grow smaller as the roundabout processes of production increase in length and *vice versa* ” (p. 69).

Thus Dr. Hayek tells us that we can take it from him that as production becomes more mechanized, employing more capital and less labour (for this is what he means by becoming more roundabout), the rate of profit—other things remaining the same—declines. We will make a note of his opinion. On Dr. Hayek's own showing, then, the garden of perpetual capitalist equilibrium, to which we were promised admission on condition that we paid the entrance fee of an initial cut in wages, contains a formidable serpent. We saw for ourselves that, no sooner was full employment restored than technical progress began to throw the workers out of their jobs again. And now we find that Dr. Hayek himself tells us that the rate of profit, that essential prime mover of the whole system, would also, *and for the same reason*, be continually declining. Now the only way in which these fatal tendencies could be offset would be, clearly enough, to cut money wage rates continually.

There is nothing more certain than that this is the inescapable conclusion of all Dr. Hayek's reasoning. There can be no question, as Professor Robbins, at any rate, seems to suggest sometimes, of constant money wages and ever rising real wages once equilibrium has been re-established. Such a wage policy would soon produce new crises by way of declining profits and declining employment.<sup>1</sup> No, if there is any efficacy in their method of *restoring* equilibrium, then precisely the same reasoning ought to show them, and does show us, that the only way of *maintaining* equilibrium will be continually to cut money wages as technical costs fall. Thus real wages will be kept constant and the rate of profit will be continually sustained.

Now at last shall we be willing to admit that, if this was done, crises would be averted and we should have a stable capitalism? Let us envisage what the situation would be. Technical progress is constantly throwing men out of the existing productive structure. Costs and prices are continually dropping. But costs are dropping faster than prices, for not only are the employers enabled to produce a given output with fewer workers, but the money rates of those still employed are continually dropping. What is happening, therefore, to the increase in net wealth that improving technique is continually giving? The employed workers are not getting it. True they are not getting poorer, for, though their money wages are dropping, so are prices: their real wages are constant. But they are certainly not getting richer. Is it not clear that under this arrangement the entire increase of wealth is going to the employers? And what are they doing with it? They are, it is assumed, re-investing it in industry. They are creating with it the capital equipment necessary to that constant technical change which was our first postulate. For this is how profits and employment can alone be maintained. These vast accumulations, amounting to the whole social increase in wealth, must be used to create new productive plants which will re-employ the workers who are continually being thrown out of the existing plants.

<sup>1</sup> A declining rate of profit and a declining level of employment are clearly the same phenomenon looked at from different points of view. The decline in the rate of profit will make it impossible to operate the less favourably situated productive plants, and so will throw their workers out of work. Similarly, growing unemployment will cause a shortage of demand, sagging prices, and so declining profits.

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Let us agree that this appears to be capitalist equilibrium found, or at any rate defined, at last. If this state of things could be perpetuated, then there would seem on the basis of Dr. Hayek's reasoning to be no reason for crises ever to recur. The holding down of real wages would free the entire increase in social wealth for accumulation. Profits would be maintained. The production of new producers' goods, the building of new factories, mines, docks, railways, etc., etc., would be on so gigantic a scale that the workers continually being thrown out of existing industry would get work.

To put it in terms of our two departments of production, fewer and ever fewer workers would get employment in the consumers' goods department. (For a constant production of consumers' goods would be maintained by fewer and fewer workers.) But more and ever more workers would get jobs in the producers' goods department. To put it in Dr. Hayek's terminology, the structure of production would grow longer and longer and longer. To put it in everyday language, the means of production would be continuously and enormously enlarged, but production itself, *viz.*, the furnishing of the great majority of the population with consumable commodities, would not increase at all.

For the first time we seem to catch a glimpse of the essential nature of capitalism. We guess that this remarkable system would, if it could be operated in its purest essence, perform one function, and one function alone. It would develop, *gigantically* and *unendingly*, the capacity to produce: but it could never pause even for a moment actually to produce—to produce, that is to say, any increased supply of consumers' goods.<sup>1</sup> It could never produce any more consumers' goods than were necessary to sustain life, efficiency, and the power of reproduction in the population.

The reasoning of its own best theorists seems to lead straight towards the conclusion that if the system relents for a moment from its task, if it devotes part of its ever growing powers, not to the development of still further powers of production, but to actually producing, it becomes involved in crises, falling profits

<sup>1</sup> Historically capitalism has not been operated "in its purest essence," it has increased the supply of consumers' goods and it has been subject to catastrophic crises. Moreover, as we shall see, the subsistence standard of life which capitalism must provide to the population may itself rise, *e.g.*, it may become necessary to produce a supply of literate instead of illiterate workers.

and chronic unemployment. Moreover, it seems that if any part of the ever growing surplus of wealth is drawn off from the capitalists,<sup>1</sup> if money wages are not continually reduced, so that real wages may be prevented from rising; if taxes are levied on the accumulations of the capitalists and distributed by way of social services to the workers, or, worst of all, if it is sought to circumvent the political difficulties of this draconian policy by inflation, the system jams: the rate of profit collapses: crisis supervenes. For any diversion of any part of the new growth of wealth from investment in new means of production throws the whole mechanism of the system out of gear. Immediately, new capital development becomes insufficient to re-employ the workers being thrown out of the existing productive structure: costs cease to fall faster than prices; there is nothing to offset the inherent sag in the rate of profit. The equilibrium equation ceases to balance. Here, then, by a short prolongation of this chain of reasoning beyond the point where the capitalist economists stop, we seem to catch sight of the true conditions of capitalist stability.

And those conditions appear to be unending and ever accelerating accumulation; an ever more rapid augmentation of the means of production. Moreover, there are indications of what this rate of accumulation must be. There is evidence that the means of production must be augmented at the rate of the accumulation of money at between 3 per cent and 5 per cent compound, if the system is not to jam.

This is a point which has much impressed contemporary American observers. Mr. Stuart Chase, Mr. Doane, Mr. Basset Jones, and others have noticed that capital resources computed in money terms, or "debts," as some of them prefer to call them, have actually increased during the capitalist era at a rate of between 3 per cent and 5 per cent compound. They observe that this must mean that the means of production must also have increased in the same progression. For stocks, shares, bonds, and

<sup>1</sup> Or, of course, by the same reasoning, if any part of this surplus is diverted from re-investment to increased luxury expenditure by the rich themselves. The pure essence of capitalism depends on the acquisitiveness of the rich so far exceeding their fleshly urges that luxury expenditure is not allowed to encroach upon accumulation and re-investment. It is easy, however, in modern conditions of great productivity to exaggerate the quantitative effects of the luxury expenditures of the rich.

the like represent the ownership of these means of production. These American observers, who are for the most part either themselves technicians, or are under the influence of technicians, are dumbfounded by their discovery. For they are convinced that, whatever may have been the case in the past, the physical means of production cannot continue to grow in this progression—at a rate, that is to say, of from 3 per cent to 5 per annum compound.

In any event how can a system survive which, it begins to appear, can only avoid periodic catastrophe if it devotes the whole of its annual increment of wealth to making it possible for wealth to grow still more rapidly the next year, *and so on to the end of time*? For the Hayek-Robbins analysis directly points to the conclusion that capitalism is a system of this kind. In order that the system should work without crisis the whole of the annual investment of capital must be devoted to the production of an increased supply of producers' goods. The supply of consumers' goods must never under any circumstances be increased.<sup>1</sup> As technical progress proceeds and it becomes possible to produce the existing quantity of consumers' goods with ever fewer workers, the workers so freed must be transferred to the producers' goods department. And this process must go on without limit, until 1 per cent of the workers of the community are employed in producing consumers' commodities for themselves and for the other 99 per cent, who are all engaged in endlessly piling up means for the production of an increased supply of consumers' goods, which, however, will never be produced, for by then only .5 per cent of the workers will be needed in the consumers' goods department and 99.5 will have been transferred to the producers' goods department—and so on to infinity.

Unquestionably there is a kind of desperate self-consistency in this picture. There is no flaw in this logic. But is it not the logic of insanity? Is not this very discovery of what appears to be the true conditions of capitalist stability a *reductio ad absurdum*, rather than a solution? If capitalism is a system which must, if it is to avoid crisis, endlessly increase the means of production, but which can never increase production itself—in the

<sup>1</sup> Except when the level of wages necessary to produce workers of the required type rises.

sense of the production of consumption goods—how can men continue to support its existence? For is not the production of consumption goods, rationally, though not capitalistically, the object of the whole business?<sup>1</sup>

It will be convenient to recapitulate the conclusions of Part I.

What kind of an impression have we gathered from our survey of the views of the various schools of capitalist economists, both amateur and professional?

The essential discovery which we have made is what these schools are quarrelling about. *They are quarrelling about how best to restore a fallen rate of profit.* Once we realize this, the merits of this internecine dispute will excite us less. Still, we shall not be able to help noticing the far higher intellectual level of the Hayek-Robbins "ultra-deflationary" school, when compared not only to the currency cranks, but to other schools of professional capitalist economists. Nor is this without significance. For, just as the insight into the nature of capitalism of the "deflationary" school is greatest, so the remedies which their analysis forces them to propose are the least practicable, the most hopeless of application. Their very theoretical realism drives them to propose the most hopelessly unrealistic practical policies. They have grasped the true conditions for the continued existence of capitalism. But they find it hard to pretend, even to themselves, that these conditions can ever be re-established. Can we wonder, then, at the almost unrelieved despair of the concluding chapter of Professor Robbins' most recent work?<sup>2</sup>

Moreover, we discovered that from another standpoint even the crudest schools of amateur economists had a final word in the argument which went far to offset their earlier rout. The professionals were easily able to show that the amateur economists' remedies would not cure the disease of glut and of crisis, but, on the contrary, would totally disorganize any system driven and controlled by profits. But the amateur economists

<sup>1</sup> The question of the extent to which this Hayekian picture of the conditions which would produce a stable capitalism does in fact correspond to any reality is dealt with in Part IV and the first chapter of Part V.

<sup>2</sup> *The Great Depression*, p. 107: "These paroxysms may pass. But the economic instability of the modern world does not seem likely to diminish. The tendencies making for instability, which we have examined in earlier chapters, have not been weakened during this depression. On the contrary, they have been strengthened." But see the whole of chapter xix.

were able to retort that in so doing the professionals had revealed a fundamental dilemma in their own case. For the professionals' remedy for our intolerable condition of poverty in the midst of plenty was to take various measures which must first intensify and then perpetuate our tragic inability to get access to the ample supply of commodities with which we could, we know, provide ourselves. Thus at the latter end there seemed to be more than a little reason to conclude that each school could refute the other. Each saw one horn of the dilemma of the antinomy of profits and plenty, but not its pair.

Finally, in our last chapter we began to feel our way towards some sort of comprehension of the true character of the capitalist system. It looked as if a short prolongation of Dr. Hayek's reasoning revealed a glimpse of the very nature of capitalism. Capitalism, we were astonished to observe, seemed to be a system which could only accumulate for the sake of future accumulation. Unparalleled in its capacity to create new and ever more wonderful means for the production of consumers' commodities, it was doomed to devote an ever shrinking fraction of its resources to their actual production. It appeared to be a powerful instrument for the process of industrializing the world. But once that task was accomplished it seemed unable to perform any other.

What are we to say of this sudden glimpse into the very nature of the system which our discussion of its disorders has revealed to us? The first thing to say is that it is only a glimpse. We have caught sight of something which may be the true and essential character of capitalism. But, again, it may not be. We cannot possibly claim to have *demonstrated* that capitalism is of this nature. We have done no more so far than suggest that it is of this nature.

Moreover, we have left many vital particular problems quite unsolved. For example, we discovered a remarkable ambiguity in the concept of costs. We noticed that there appeared to be two ways of cutting costs. You could improve the technique of production, or you could reduce wage rates, etc. But on further examination an improvement in the technique of production turned out to be nothing else but production with fewer workers. Hence the two ways of reducing costs appeared to consist either of paying fewer workers at the same wage rates or the same number of workers at lower wage rates. This



discovery certainly seemed to indicate that labour costs were a very inclusive sort of costs in the last analysis. But it was far from clearing up the problem.

Most important of all, however, was our inability to do more than indicate a cause for that all important phenomenon, the tendency for the rate of profit to decline. We found ample evidence that the rate of profit does decline. It does not do so, it is true, in any even, steady way, but by a process of sudden and catastrophic collapses, which we called crises. And we found that Dr. Hayek's analysis seemed adequate to explain why the decline took this highly uneven, oscillating form. But we found that analysis quite inadequate to account for the fact of the decline itself. We were able, it is true, to understand that a decline in profits in a period of the rapid growth of potential plenty was not unexpected, since profits and scarcity seemed to be associated in some way. But all this was very vague. And finally we made a note of Dr. Hayek's own declaration that the rate of profits does fall, although he had not the space to tell us why.

So far we are certainly open to the charge that after discussing the alternative explanations of the nature of capitalism and its crises we have offered no solid or satisfactory explanation ourselves. And yet the prospects offered by proceeding further along our present line of approach do not seem promising. Can it be that this whole approach can at best take us to within sight of a solution of our problem?

For what approach have we been following? We have so far followed the general line of approach of the various schools of capitalist economists. We have adopted the categories and concepts of economic thought with which we found them to be working. And yet, as we saw at the outset of our enquiry, the main *corpus* of modern capitalist economics has been developed by ignoring the very existence of our problem. Contemporary capitalist economics, as such, knows nothing of the existence of crises. Contemporary capitalist economists such as Dr. Hayek, Professor Robbins, or Mr. Keynes, can only approach the problem at all by a sort of back door, by taking up the detached special subject of monetary theory. Was it not to be expected, then, that the use of the categories and concepts of modern capitalist economics would lead to but inconclusive results? Is it not

probable that before we can solve our problem we shall have to find a new line of approach altogether? Do we not need, above all, the categories and concepts of some *corpus* of economic theory which has found it possible to take cognizance of the phenomena of recurrent crises?

The experience of this section of our argument has shown us that we need new and more powerful equipment for the task which we have set ourselves. We shall be well advised, before making another attempt upon the problem of capitalist crisis, to go in search of a new set of economic categories and concepts.

#### SUMMARY OF CHAPTER VII

A restoration of the rate of profit seen by all professional capitalist economists as a pre-requisite of recovery. They differ only as to method. A paradox discerned in raising the rate of profit as a method of achieving recovery in the sense of plenty. Profits increased by high prices and low costs. Plenty increased by low prices and high costs. The antinomy of profits and plenty. Mr. Chase's glimpse of the truth. His failure to face the overriding necessity of maintaining profits. This failure typical of all credit cranks.

The capitalist economists promise plenty as well as profits in the end. Purchasing power increased in spite of lower wages by increased employment. Their claim that this will produce permanent and progressive equilibrium. Their claim refuted from their own line of reasoning.

The renewed tendency to disemployment and falling profits. These tendencies only to be offset by continuing cuts in money wages, thus keeping real wages constant. Would this be capitalist equilibrium discovered at last? Conditions of this supposed equilibrium rehearsed. An unending and ever accelerating process of accumulation seen to be the chief condition. American statisticians dumbfounded by their own discoveries. Essential nature of the capitalist system distantly discerned. Its nature to augment unendingly the means of production, but never to augment the production of consumers' commodities.

Recapitulation of Part I. Inconclusive character of our analysis. Do we not need a new set of economic categories and concepts?

PART II

FROM POLITICAL ECONOMY  
TO ECONOMICS

“ ‘ Economics ’ and ‘ Political Economy ’ are something more than differences of name : they are different enquiries, differing in scope and aim.”

(Maurice Dobb, *An Introduction to Economics*.)



## CHAPTER VIII

### *Costs and Values*

IN preceding chapters the concept of costs has been continually employed. We saw that it was common ground between everyone, from Major Douglas to Dr. Hayek, that the capitalist system could not continue to function unless the prices realized for commodities exceeded, on the average, their costs of production. Again, our various refutations of Major Douglas may be tersely expressed in another way. We may say that Major Douglas, in failing to distinguish producers' from consumers' goods, neglects some nine-tenths of the total costs of production. For producers' goods, in a rationally organized society, would be regarded as but necessary means to the production of consumers' goods. Producers' goods would be considered as a necessary debit in the community's account. Our net wealth consists alone in the consumers' goods which they (the producers' goods) enable us to make. This is why Major Douglas has the pleasant delusion that we are, here and now, some ten times richer than we are. He has, as it were, mistaken the *gross* output of the productive system for its *net* output. He has not realized that nine-tenths of the things made and sold are necessary to the production of the final tenth: but that this final tenth is all we can actually consume. He has not deducted nine-tenths of the total costs of production from the total product of society as a whole.<sup>1</sup>

Again the "professionals" can refute Mr. Hobson and Professor Fisher by the use of the concept of falling costs alone. What these two gentlemen say would be perfectly correct if it were not for the fact that technical progress is continually reducing costs as well as prices. Finally, Dr. Hayek's analysis depends upon the existence of this continuous fall in costs of production, and his programme for recovery is based upon measures designed to accelerate it. Costs, he urges, must be driven down still faster by wage cuts, cuts in social services, and other such measures.

<sup>1</sup> This is not to say that in a rationally organized society which was devoting its energies to maximizing the present and future production of consumers' goods (in a reasonable proportion) we might not rapidly become as rich as Major Douglas thinks we are now.

It was at this point in the argument that we found ourselves involved in difficulties over the concept of costs. In discussing the American New Deal, for example, we said that in one sense costs *were* falling rapidly (from technical change) and that it was this neglected fact which made Mr. Roosevelt's programme so extremely inflationary and, therefore, crisis-begetting. Yet in another sense we agreed that the New Deal had failed to reduce costs, in the sense of wage costs, and we claimed that this, again, was what made the New Deal so obviously preparatory to a new crash. We were near, then, to self-contradiction. We were attacking the New Deal both because it ignored the fall in one kind of costs and because it failed to reduce another kind of costs. We found it necessary to begin to split up our general concept of costs into the two categories of "technical costs" and "wage costs." And it seemed to make all the difference which of these kinds of costs you reduced.

Then, again, we got into trouble when, in pointing out the antinomy between profits and plenty, we suggested that, while high prices and low costs spelt profits, low prices and high costs spelt plenty. We had to add a footnote agreeing that it was only high wage costs which made for plenty. Needless to say, high technical costs, such as an unnecessarily large and wasteful use of raw materials, do not make for plenty. As a rough and ready solution of the difficulty we defined a drop in wage costs as the production of a given output with the same number of workers paid at lower rates. A drop in technical costs, on the other hand, was the production of a given output with fewer workers paid at the same rates.

This definition seemed to fill the bill. But is it really justified? Does all technical progress amount to nothing more than the production of a given output with fewer workers? If so, it will be noticed, all costs are in the last analysis wage costs. For if one way of reducing costs consists in giving each worker less, and the other way consists in reducing the number of workers paid at all, both are ways of reducing the total wages bill. But is this correct? It is becoming increasingly obvious that we cannot go on with the enquiry until we have cleared up this concept of costs. It underlies the whole of our argument. And yet we have no precise notion of what costs are. It will not do to

go on regarding them quite simply, as we did at first, in terms of money. We cannot rest content with saying that costs are the sums of money which have to be paid out in production. For our own argument has led us to the conclusion that it makes all the difference whether these sums of money are reduced by paying fewer workers at the same rates or the same number of workers at lower rates.

In any case, we cannot possibly suppose that the sums of money paid out in the course of a particular process of production themselves *constitute* what that process of production has cost. We all know that what the sums of money do is to *measure* what that process has cost. There must be something (some economists have called it "the real costs of production") which the money measures. We have only to think of a very simple economy carried on without money to demonstrate this. If a group of ten people carry on production, and exchange the products among themselves by direct barter, without using any money, it will certainly not mean that they have no costs of production. (Crusoe himself was not so fortunate.) It will cost them something to grow their food, something to weave their clothes. Moreover, they will have to make an attempt to calculate what these costs are. They will have to do so, for instance, when they come to consider whether some change in their way of production will pay them or not. Let us say that they have to make up their minds as to whether it will pay them to make a new and improved plough or to carry on with their present one. They will have to try and find out the way in which they will get most food with least trouble. Will, in other words, the new plough reduce the cost of producing their food more than it will itself cost to make? But what are these costs? Obviously they are not money. Money is merely their measure.

What, then, are costs?

It would not be too much to say that in order to answer that question adequately it would be necessary to write a history of economic thought.<sup>1</sup> Indeed, as we shall see, a history of capitalist

<sup>1</sup> A task awaiting some Marxist scholar. Why has Marx's own *Theorien über der Werth* not been continued to cover the late nineteenth-century and early twentieth-century capitalist economists? Mr. Maurice Dobb's essay, from which we have already quoted, is the only English work in the field. Its fault is its brevity. Its readers will see, however, how much this part of the present volume owes to it.

economic thought would not provide any satisfactory definition of costs. What are costs, the jesting professors have certainly asked? But they have not stayed for an answer. And yet the question of costs is clearly of unsurpassed importance. For, after all, what we are all interested in is not the *gross* product of the productive system, but the *net*. There is obviously some negative quantity in economics. Just as there is a positive quantity—"goods"—there must be a negative quantity—"ills." Just as there is utility there must be disutility. For all production uses up something. And if it uses up too much we say that it becomes "not worth while," or that "it does not pay." Hence what we are interested in is the balance between what the productive process uses up and what it produces. Production is the production of a surplus over and above what the process uses up. Without such a surplus, such a *net* product, the whole process is pointless.

This is very easy to see when the productive process uses up the same commodity which it produces. It is very easy to see, for example, in the case of agriculture. You plant, let us say, ten bushels of seed corn. You harvest thirty bushels. How many bushels have you produced? Thirty? Surely not, for, unless you are going out of business, you must put aside ten bushels for next year's seed. Now say there is a drought. Your harvest is only ten bushels. Have you produced anything? Scarcely. It would obviously have paid you better to sell, store, or eat your ten bushels of seed corn. For your seed corn was not your only cost of production. There was the labour, the manure, etc., etc. A ten bushel harvest from ten bushels of seed means a net loss. So far from being production, it is destruction.

The fathers of political economy, the Physiocrats, had a tight hold on these truths. The Physiocrats, let it not be forgotten, were a part of the great school of enlightenment of eighteenth-century France, a school the concepts of which have remained in many respects the unsurpassed achievement of capitalist culture. Since agricultural production was the predominant form of production in their society, the Physiocrats devoted most of their attention to it. And they saw that what mattered was not how much corn you raised, *but how much more*



corn you raised than you sowed.<sup>1</sup> This margin they called *le produit net*. The seed corn, and the other necessary "factors of production," as we should say, used up in growing it, they called *le prix nécessaire*. Many economists and economic historians have grossly misunderstood the Physiocrats. But few indeed have improved upon these basic categories of *produit net* and *prix nécessaire*.

It was easier for the Physiocrats to keep hold of this concept than it has been for later economists. The Physiocrats, looking out upon the *prairie* of eighteenth-century France, could observe the necessity of setting aside the seed corn. They could see vividly that the whole gross product was not available for consumption. As we have noticed, however, even in agriculture the seed corn was not the only cost of production. There was the manure; there was the maintenance of a stock of agricultural implements; there was the food for the men and women who used these implements from harvest to harvest. Hence, the Physiocrats saw that for there to be genuine production, a genuine surplus, a *produit net*, the harvest must produce enough corn, not only to replace the seed, but to feed the workers till the next harvest, and to allow of some corn being sold from time to time, to replace the ploughs, etc., as they wore out, and to pay for the workers' clothes and the like. Indeed, if the harvest only just sufficed for these purposes there would still be no *produit net*. The *produit net*, the surplus, only began when all these necessary purposes had been served. But if there were, say, five bushels over and above that amount, then this was the *produit net*. And what was done with this *produit net*? It could be used to increase the amount of seed corn, to sow a bigger area for next year: in more general terms, to increase the scale of agricultural production. Or it could be used for the support of people other than the agricultural workers. It, and it alone, could be taken by the landlords for rent or by the Government for taxes. It was so taken. And economic progress consisted in increasing this surplus to the utmost possible extent.<sup>2</sup>

<sup>1</sup> Or, more exactly, how much more corn you produced than you used in the whole process of producing your corn.

<sup>2</sup> The reader will be struck by the identity of this view with the doctrine of Dr. Hayek. For the Physiocrats, as for the very latest school of capitalist economists, the subsistence of the workers is part of the cost of production—nothing more and nothing less. All increments of wealth must go to non-workers for accumulation.

We have said that it was easy for the Physiocrats, contemplating agricultural production, to keep a tight hold on the idea of "real cost," or, as they called it, a *prix nécessaire*, and of a surplus above this cost, or a *produit net*. For it will be seen that this concept depends upon comparing one quantity of commodities with another. You put, on the one hand, the commodities which you have used up in production and, on the other, the commodities which you have produced. And if the second heap of commodities is bigger than the first, you say that there has been a *produit net*, or surplus. Now there is not the slightest difficulty about doing this in the case of the seed corn. Ten bushels were used up. Thirty bushels were produced. But we saw that, even in the case of agriculture, more than the seed corn was used up in the process of production. There was some wear and tear of implements, some manure, and subsistence for the workers. The heap of commodities used up was heterogeneous. It consisted of, say, one-fiftieth part of a plough, ten bushels of corn for seed, fifteen bushels for workers' subsistence, and a load of dung. How do we compare this heap with the heap of thirty bushels of corn harvested? How do we decide which is the larger?

We know that it is possible to decide which is the larger. For we do it every day by means of the market. We see whether the commodities which we have produced will or will not "fetch" (whatever that term may mean) more than the commodities which we have used up. But *how* does the market do this? How are the respective magnitudes of the heaps of heterogeneous commodities determined? Here was a problem even for the Physiocrats. But reflect upon the nature of this problem in modern, highly complex, highly industrialized conditions. Costs, it appears, are made up of the commodities used up in the process of production. Hence, when we want to arrive at an estimate of costs we must total up the commodities used in any given process of production. Not until we have got this total can we compare it with the total of commodities produced. Or again if, like our ten colonists, we are contemplating a change in productive methods, it is this total of commodities used up in production which we must compare with another total of commodities which would have been used up producing the same product by

a different method. Unless we can make up these totals, we cannot compare the costs of two different methods of production.

So the very concept of costs depends upon our ability to add up and then compare quantities, totals, of commodities. And how, pray, do we do that? Commodities, remember, are goods or services. They are anything which is bought and sold on the market. How, then, are we to compare the size of two different totals, two heaps of commodities? How shall we say which heap is the larger? Let us take an example. Let us take as one heap of commodities what a particular skilled worker, say a dentist, sells in a week. Let us say that he "sells" twenty fillings and five extractions. Then let us take as the other heap what the dentist buys in the same week. Let us say that he buys four pounds of meat, ten pounds of potatoes, three pounds of cabbages, ten pounds of bread, two shirts and a pair of socks, one week's occupancy of his house, a seat at the cinema, fifty cigarettes, one book, and six tennis balls, plus the raw materials of the fillings and the upkeep of his instruments. Which of these heaps, aggregates, totals, or quantities, of commodities is the bigger?<sup>1</sup> It is the same with a process of production. Let us take the cinema industry. Let us suppose that, amongst other things, the following commodities are used up in the production of Miss Garbo's next film—one mile of celluloid, one camera, with speaking apparatus, worn out, two aeroplanes (hire of), 10,000 kilowatt hours of electrical energy, one million man-or-woman-hours of unskilled labour, ten thousand man-or-woman-hours of skilled labour (etc., etc., etc.). Which is the larger—whatever "larger" means in this sense—this aggregate of commodities or Miss Garbo's film?

The business of comparing the size of the aggregate of commodities used up in production with the final product is evidently not so easy, once you leave behind the simplicities of seed corn and harvested corn. How can we possibly say that any one lot of commodities is bigger than any other? How can we say that there is more in one heap than in the other? More what? The final product may be one single commodity—a locomotive.

<sup>1</sup> The poet wondered what the vintners bought one half so precious as the thing they sold. So even the Persians were worried by this question of how it is that we compare the magnitude of the aggregate of commodities which a man sells with what he buys.

Dozens of commodities may have been used up in its production. Yet you would not say that the locomotive had cost more to produce than it was worth on that account. Is it impossible, then, to compare aggregates of commodities? Are commodities what the mathematicians call incommensurables? Apparently so. For, in order to compare the magnitudes of things, they must have some common factor. It must be possible to express all the qualitative differences between them as quantitative differences. It must be possible to say of one aggregate that it is equal to, say, 15 units of something, and of the other that it is equal to 12 units of the same thing. But what conceivable common factor have such diverse commodities as dentists' extractions, cabbages, performances of Miss Garbo's film, rides in buses, shirts, and books on economics?

Commodities, then, are incommensurable? But this, we know, cannot be true. For, in fact, we compare the magnitude of aggregates of commodities every day of our lives. Take the two examples which we have contemplated. The dentist will certainly compare the aggregate of commodities which he has sold during the week with the aggregate of commodities which he has bought. He will, in every-day language, compare his income with his expenditure. He will perform, in the most matter of fact way, the apparent miracle of deciding which is the larger heap—the heap consisting of the food, clothes, shelter, amusements, and the like, which he has bought, and the heap consisting of the fillings and extractions which he has sold. He will compare them by expressing each heap as a total of money. He will say that the fillings and extractions were worth, say, £15, and the purchases £12. In the same way the cinema corporation which employs Miss Garbo takes great care to add up the amount of money which it has had to spend on the commodities used up in the production of her film, and compares this total with the amount for which it is able to sell or hire out that film.

There is not the slightest doubt, then, that we do compare the magnitude of aggregates of commodities, however diverse. But how do we do it?

It is no use simply saying that we do it by comparing each heap or aggregate of commodities to money. Money is, or

represents, gold.<sup>1</sup> And it will not help in the least to say that we compare each heap of commodities to a heap of gold. What possible connection is there between, say, a seat at the cinema, plus ten oranges, plus three treatises on economics, and one ounce of gold? What shred of meaning is there in saying that the sum of these commodities is "more" or "less" than the ounce of gold? No, money is obviously no more than the scale by which we measure off the units of some more fundamental something which must be common to all commodities. What is this something?

Now economists, as everybody knows, have always answered this question (when they have taken the trouble to formulate it) by saying that this something common to all commodities was value. The utility of this information is diminished, however, when we recollect that various schools of economists have defined value differently. They have achieved agreement on a name for the factor common to commodities—but on little more.

The fathers of economic thought, the Physiocrats, and their immediate successors, the giants of what is called the classical school, said that value was determined by labour. They said that the "more fundamental something" which was common to all commodities, and which alone made it possible to compare their magnitudes, was the fact that they were all produced by an expenditure of human labour. This was what made them "valuable." Commodities, they said, were *composed* of human labour. When we added up heaps of commodities we made a total of so many units of human labour. And the units of human labour were time units. A heap of commodities added up to say 15 hours of human labour. For it had taken 15 hours of human labour to produce it. The fact that they had all been produced by the expenditure of a given quantity of human labour was that "more fundamental something" which was common to all commodities. Human labour was, in other words, that negative quantity, that cost, which we groped for just now. Human labour was what we wished to minimize, just as wealth was what we wished to maximize. Human labour was "illth" as opposed to wealth. It was the "ill" which had to be created

<sup>1</sup> When money is inconvertible paper, or the intangible figures of a bank deposit, the difficulty is obviously even greater.

in the production of every "good." What made things valuable was that they could only be obtained at a cost : at the cost of the expenditure of a given quantity of labour. This was the unchallenged theory of value of the Physiocrats, of Adam Smith, of Ricardo, and of all the economists until almost exactly a hundred years ago. It was, in a developed form, the theory of value of Marx, and it is the theory of value of Marxist economists to-day.

#### SUMMARY OF CHAPTER VIII

The essential nature of the concept of costs. The concept of falling costs necessary to a refutation of the under-consumptionists. The concept of costs split up into "technical costs" and "wage costs" during our consideration of the New Deal. Necessity to clear up the concept of costs before the enquiry can proceed. What are costs ? There must be some negative economic quantity. What is it that production uses up ? The seed corn must be subtracted from the harvest in order to get the net amount of corn produced. The Physiocrats. *Produit net* and *prix nécessaire*. Production not worth while unless a *produit net* or surplus is realized.

But this conception involves comparing two aggregates or heaps of commodities. This is not so simple in modern conditions. Two modern examples. What the dentist sells and what the dentist buys. Has Miss Garbo a *produit net* ?

But we do continually add up commodities and compare the aggregates so formed. How do we do it ? Not just by comparing them to an amount of gold. There must be a common factor. What is it ? The economists have called this common factor value. What, then, is value ?

No agreement amongst capitalist economists as to the nature of value. For the classical school of capitalist economists and for Marx labour is value.

## CHAPTER IX

### *The Heyday of Capitalist Economics*

JUST over one hundred years ago there arose a new school of capitalist economists. This school may be said to have begun with William Nassau Senior and to have ended with Alfred Marshall. Senior<sup>1</sup> became dissatisfied with the labour theory of value. For it became apparent that the labour theory of value, in the form in which it was enunciated by the classical economists, was unable to give a satisfactory explanation of the phenomenon of profit. The worker, the theory held, sold his labour embodied in a commodity. The peasant small-holder, employing no hired labour, was the type of this worker. If society had consisted exclusively of such small-holders, each producing, say, one agricultural speciality, the first wheat, the second potatoes, the third fruit, and so on, plus a few independent artisans cobbling their shoes or making their spades, then the labour theory of value would have been almost self-evident.

In such a society, it is clear, the ratios of exchange between the wheat, the potatoes, the boots, and the spades could depend on nothing else than the expenditure of labour, measured by time, which the production of each commodity necessitated. And it was in the eighteenth century, when society bore some recognizable resemblance to this picture, that the labour theory of value was evolved.<sup>2</sup>

For it was apparent to the eighteenth-century economists that what men were selling when they sold their commodities were embodied, materialized hours of their labour. This was what they meant when they said that men were selling their labour. It is necessary to get this perfectly clear because the typical way in which production is organized to-day is so different from what it was two hundred years ago that the phrase "a man selling his labour" calls up to us a very different

<sup>1</sup> Again it is convenient to pick out a spokesman. But, as usual, the truth is that several capitalist economists made similar moves at about the same time.

<sup>2</sup> Early eighteenth-century society resembled, rather, this picture, with a class of landlords and their dependants superimposed upon the small, independent commodity producers, and drawing rent from them. But the labour theory of value was able to account for rent quite satisfactorily (see p. 178) by pointing to the monopoly of land possessed by the landlords. Rent, it was shown, was in essence a simple tribute extracted by the possessors of this monopoly.

concept. If we are told that a man has sold twelve hours of his labour we think of him having contracted to work for someone for twelve hours. But, as we have just seen, this was not at all what the classical economists had in mind when they spoke of men selling their labours. They had in mind workers who worked for themselves on their own farms or in their own backyards and then sold the products of this work on the market. And if this is the operation to which we refer when we speak of a man selling his labour, then it is clear that a man cannot sell his labour unless and until he can perform this labour ; unless and until he can work on his farm or in his backyard. For a man could only sell, the classical economists maintained, actually completed, finished labour which had become embodied into a commodity. Unless we understand that this, and not the to us far more familiar and natural conception of a man hiring himself out for pay, is what the classical economists meant by a man selling his labour, we shall never be able to understand either the controversy between them and the post-classical capitalist economists, or Marx's solution of the problem.

By the end of the eighteenth century, however, the nature of society had already greatly changed. The characteristic form of the organization of the main productive processes had ceased to be that of simple, independent producers, producing by their own labour commodities which they then took and sold on the market. Both in farming and manufacture the characteristic producer had become an employer of other people's labour. The typical farmer who now brought his wheat, his potatoes, or his fruit to market was not a small-holder ; he was an employer of a group of labourers who themselves owned no land, and, therefore, could independently labour to produce nothing. The typical maker of agricultural implements had ceased to be an independent artisan and had become the employer of a group of workers, brought together in his workshop and using his raw materials and tools.

Now what effect did this change in the way production was organized have on the labour theory of value ? In the first place, it ceased to be obvious that the commodities produced in this new way would exchange in proportion to the amount of labour embodied in them. For the men and women who had



actually made them with their own hands did not sell them. On the contrary, they were sold by the employer. And he paid a wage to the workers who made them which might or might not correspond in amount to the price at which he was able to sell the commodities.

It seemed that the question of whether the labour theory of value remained true in the new conditions depended upon whether in fact the amount of money paid in wages in the production of a commodity turned out to be the same as the price at which it was sold. For if it did, then, clearly, the labour theory of value could still be shown to be true. For it would still be true that the workers would sell their labour embodied in a product, only now they would do so indirectly, *through* the employer. But, as everybody knows, the amount of wages paid out in the production of even a primary product is not the sum at which an employer sells a commodity. He must, and does, sell it at this amount plus some profit on his capital.<sup>1</sup> Now where, on the labour theory of value, did this profit come from? Profit appeared, it could be shown, whether or not the employer himself worked either by hand or brain in the production of the commodity. It did not appear to be drawn from the *force majeure* of monopoly rights as was the landlords' rent. Where did profit come from then?

It was, in the final analysis, this simple question which destroyed the labour theory of value in its original form. For the only way by which the appearance of this new phenomenon, *viz.*, the profit of an employer of labour, could be accounted for, it seemed to the economists, was by abandoning the hypothesis that it was human labour alone which created value. Once that step was taken, it seemed easy to account for the employer's profit. Surely, Senior and his colleagues pointed out, there was another factor necessary to production as well as labour: there was capital. And profit was acquired by the employer in virtue of the fact that he provided this other factor: that he provided capital. He provided the essential instruments of production without which nothing could be accomplished. And where had

<sup>1</sup> For simplicity's sake we are envisaging a commodity such as coal for the production of which the employer need provide no raw material. In fact, the raw material is as much a part of the employer's capital as are the instruments of production.

he got his capital from ? He had got it, said the economists, by saving up instead of consuming some commodities.

For capital was created by saving (as we noticed in Part I). Capital was the result of people saving or abstaining from consumption. Thus resources which might have been consumed by individuals here and now were preserved. And they were preserved in order that they might be made use of for the purposes of future production. The seed corn example is again relevant. Ten bushels out of the crop of thirty must be set aside if the next year's sowing is to be as big as last year's. But the farmer may, if he likes, set aside, instead of eating or selling, another two bushels for seed, and plant twelve bushels next year. If so, he increases his working capital by two bushels, and he does so by abstaining from consuming them. Was not this act of abstinence just as necessary to the production of the next year's harvest as was the labour ? It was, said Senior. Hence the "real cost" or value of a commodity had to be measured by the labour used in producing it, *plus the "abstinence"* needed to create the capital which had also been used in producing it.

The members of the new school did not at once realize the profound change which they were thus making in the very foundation of economic science. It is easy for us to see, however, that by admitting "abstinence" as a constituent part of "real costs," they changed the nature of that "more fundamental something" of which commodities, we found, must be made up. (For unless they were made up of some one thing we could not, as we do constantly, compare their magnitudes.) And not only did the new school change the nature of this basic factor common to all commodities ; they, apparently, destroyed its unity. Commodities were not now said to be made up of the amount of labour which had gone to make them, but of the amount of labour plus the amount of abstinence which had gone to make them. The conception was developed by successive economists until Alfred Marshall gave it its final shape. And it is in this final shape that we shall best see its full bearings. Here is Marshall's theory of "real costs."

"The exertion of all the different kinds of labour that are directly or indirectly involved in making it, together with the

abstinence, or rather the waitings, required for saving the capital used in making it : all these efforts and sacrifices together will be called the real cost of production of the commodity. The sum of money which has to be paid for these efforts and sacrifices will be called either its money costs of production or its expenses of production ; they are the prices which have to be paid in order to call forth an adequate supply of the efforts and waitings that are required for making it : or, in other words, they are its supply price."<sup>1</sup>

We notice how careful Marshall is to make it clear that he realizes that the money paid out in the course of the production of a commodity only *measures* the real cost of that commodity ; how fully he endorses our contention that there must be a more fundamental something (or somethings) for the money to measure. And he defines these more fundamental somethings, the quantity of which money measures, as " a supply of efforts and waitings."

What are we to say to this new theory of costs ? We must keep firmly in mind the reason which has driven us to undertake our expedition in search of a theory of costs. We have found that it is absolutely essential to be able to add up heaps of commodities and make a total which means something. We had to do so a dozen times in the course of the argument of Part I. Moreover, we do so in practice every day of our lives. And yet we find it impossible to conceive of *how* we do so unless commodities have some common factor which makes them commensurable. That common factor, say (or rather, as we shall see, said) the capitalist economists, is their value. It is the *value* of the various commodities which we add up, both in practice and in theory.

What, then, is value ? The value of a commodity, said all economists up till about a hundred years ago, was the amount of labour, measured by time, which had had to be used in making it. So, in the last analysis, when we added up heaps of commodities, we added up the number of hours of labour which it had taken to make the whole heap. Now this may or may not have been true. But, at any rate, it was clear cut and definite. But now we find that about a hundred years ago the capitalist economists abandoned

<sup>1</sup> This passage is elucidated by Mr. Dobb in his *Introduction to Economics*.

this view. They now tell us that the value, or the "real cost," of a commodity, is made up, not of labour alone, but of labour plus abstinence : or, as Marshall finally formulated it, of "a supply of efforts and waitings." "A supply of efforts and waitings." Let us allow that idea to sink into our minds. Here we have another aggregate. A sum, or total, made up of two factors, namely, efforts and waitings. Now what is the answer to an addition sum made up of efforts and waitings? Is it 55, for example? And, if so, 55 whats? Are we not in trouble with incommensurables again? What greater sense is there in adding an "effort" to a "waiting" than there is in adding a pound of tea to the equator? It seems that in admitting "waitings"—(and remember that "waitings" are, in fact, capital) as an additional cause of value, as a "real cost," the latter day capitalist economists have made the concept of value useless for our purpose of providing an explanation of what it is that we add up when we add up commodities. They have a further suggestion, however. Have we not overlooked a real common factor between "efforts" and "waitings"? Are they not, in fact, both sacrifices? Marshall himself also speaks, we notice, of "efforts and sacrifices." Is not this, then, the common factor? Does not the real cost of a commodity, its value, consist then, in the amount of sacrifice, literally the amount of unpleasantness, which its production has cost people?

Let us exemplify. Say that a capitalist puts up £1,000 worth of capital in order to make a certain commodity. This means that he abstains from spending his £1,000. He waits. Hence he is said to make a sacrifice measured by £1,000. The workers who made the commodity are paid, say, £100. Their sacrifice consisted in the efforts of brain and muscle which they expended instead of lying in bed or going to the pictures. And their sacrifice is measured by £100. Here, then, after all, is another single common factor. The real costs of a commodity are measured by people's disinclination to make the efforts, or to forgo the expenditure, necessary to the production of that commodity.

This theory of costs is the natural and inevitable counterpart of what is called "the subjective theory of value." We shall come to this new theory of value, which the capitalist economists of the last hundred years gradually evolved, in a moment. In the

meanwhile, we must point out how completely subjective is this theory of real costs. In this case also, we repeat, there is no attempt to make money itself more than the measure of costs. This theory of costs, just as much as the labour theory, is compelled to seek for that "more fundamental something" which the money costs of production only measure. And it finds it in sacrifice, in disinclination, in unpleasantness. A thing costs, this theory declares, the amount of unpleasantness which it has taken to create it. It is worth the precise amount of the disinclination for work experienced by all the workers engaged in producing it, plus the precise amount of the disinclination to invest the necessary capital, instead of spending it, experienced by the capitalist. And, once again, what money does is to provide us with a means of measuring these quantities of disinclination. But for this purpose it is said to be infallible. It might, at first sight, have been thought a somewhat difficult task to measure accurately a capitalist's conflicting impulses, as to whether to invest £1,000 or to spend it on a swimming pool. Equally it might have been thought difficult to say just what quantity of disinclination to get up a worker felt when the buzzer rang in the morning. These might have been supposed to be tasks for the psycho-analyst alone. Yet these are the quantities which have, on this theory, to be added up in order to find the real cost of commodities and so render them commensurable. In practice, however, the capitalist economists tell us (or used to tell us), there is no difficulty. We have conclusive evidence of the exact amount of disinclination experienced by capitalists and workers alike. For we know the amount of money which is needed to overcome their disinclination. Hence these amounts of money measure exactly the quantities of the disinclination. These amounts of money are, as Marshall says, what "have to be paid in order to call forth an adequate supply of the efforts and waitings."

The new school of capitalist economists claimed, then, that the money which actually had to be offered to the capitalists in order that they should wait, and to the workers in order that they should work, provided us with an exact measure of the sacrifices which production necessitated from each of them. The practical deductions which can be made from this theorem

are, evidently, of the highest importance. If it is a fact that the money which must be given to the capitalists for waiting, for postponing immediate consumption, that is to say, and thus using their resources instead for future production, and to the workers for working, does exactly compensate each of them for the amount of sacrifice which each has to undergo, then our present economic arrangements are, in fact, perfect. They minimize, that is to say, the amount of unpleasantness which we all must undergo in order to produce a given output of commodities. (Or, rather, they would be perfect were it not for the misguided interference of governments, trade unions, monopolists, etc., with the free play of the market.)

The money offers which have to be made to induce the capitalists to invest and the workers to work are, it is alleged, perfect expressions of the free, voluntary choices of individuals. Until and unless the capitalist is paid just a little more than what will compensate him for the sacrifice involved in investing instead of spending, he will spend. Until and unless the worker is paid just a little more than what will compensate him for the sacrifice involved in working, he will remain idle. Hence any interference with the free play of the market will reduce the amount of "net satisfactions" obtained by society. For instance, if trade union action, or minimum wage legislation, forbids the worker to accept a certain wage, there must be a net reduction in his satisfaction. For unless the wage offered is big enough to more than compensate the worker for working, he will refuse it in any case, and there will be no need for trade union or trade board. If, on the other hand, the wage offered does more than compensate him for his sacrifice of leisure, and he is forbidden to accept it, his net satisfactions will be decreased.

This general principle that the play of the market, if left to itself, must maximize net satisfactions was, of course, widely extended. It was used to explain much more than costs. As the famous theory of marginal utility it became the apologetic of every aspect of the existing economic system. There is no need to rehearse its various applications : how it regulated the supply of factors of production between different industries : how it explained fluctuations in the rate of interest, etc., etc. This is,

in fact, that main *corpus* of capitalist economics which, as we have seen, is not germane to our subject of enquiry. But it is necessary to recall its most common application of all.

We have given an account of the late nineteenth-century theory of real costs, as finally expressed by Alfred Marshall. And we have noticed that this theory of costs replaced the labour theory of value of the classical school. Had the late nineteenth-century economists, then, no theory of value? They had. As a school they adhered to the above-mentioned subjective theory of value. We have seen that their theory of costs was essentially subjective. In this respect it was only one side of their theory of value. And their theory of value placed its emphasis, not on costs at all, but on demand. What gave a commodity its value was, basically, that there was a demand for it. And there was a demand for it because it satisfied some human need. Accordingly, you could determine a commodity's value by the amount of it which was demanded. More precisely, a commodity's value depended upon how high it stood on people's list of preferences. This list of preferences the economists called the consumer's "demand schedule." A commodity's value (and price) depended basically upon how high a commodity stood on this list. The more it was preferred, the higher would go its value and price. For, if it was highly valued, only a high price would allot the available supply of it to the various consumers who were bidding for it.

Reflection will show that this determination of value by demand is only the other side of the determination of costs by sacrifices. Sacrifices are the negative side of demand. Demand is demand for satisfactions or pleasures. Sacrifice is the undergoing of pain. It is true that in post-classical economic theory the value of a commodity was usually said to depend upon supply and demand. But the demand for it depended on its ability to afford pleasure, and its supply depended upon the amount of pain necessary for its production. Hence its value depended upon the ratio of the pleasure it could give compared to the pain necessary to its production. Different economists gave different names to these subjective psychical quantities upon the ratio of which their theory of value depended. Jevons spoke of utility and disutility: others of "satisfactions" or of pleasures and sacrifices:

others, quaintly, with Marshall, of "efforts and waitings" instead of pain; but these were merely terminological differences.

Now just as we found that in the theory of costs, the unpleasantness, the disinclination, which had to be overcome in order to get production going, could be measured exactly, it was said, by the amount of money which had to be paid out in the process of production, so, according to the subjective theory of value, the quantity of pleasure which a commodity would give, its capacity to supply human needs, was measured by the amount of money people would pay for it.

The practical significance of this point is similarly great. For again we realize that the theory has led us to the conclusion that the existing money offers which are made for commodities do express precisely and accurately the degree to which particular commodities satisfy a human need. And so, once again, we are assured that our existing arrangements, if undisturbed, or if freed from existing interference, will be certain to maximize "net satisfaction" or "utility." The money offers which are actually made are sufficient evidence—indeed, they are the only evidence which we can ever have—of what people really need. If more people demand more motor-cars and less people demand less milk, up goes the price of motor-cars and down goes the price of milk. Soon factors of production are moved from agriculture to engineering. More motor-cars and less milk are produced. And this is precisely as it should be. The consumers' preference has spoken. The money offers have shown that more "utility," more "net satisfaction," will be produced if so many thousand agricultural workers move into towns and begin making motor-cars. And attempts to deny that these money offers are perfect expressions, the only expressions we can have, at any rate, of people's real needs are inadmissible. They will only result in a senseless effort to dictate to people what they should buy: to produce things that people do not want. The effective demand of the market is the spontaneous expression of human needs. Anything but perfect obedience to it must decrease the degree to which production meets these needs.

This identification of effective demand, as expressed by money offers on the market, with human needs and desires; and this acceptance of the money costs of production as a true measure



of the real human sacrifices involved in production, was the essential theorem of the capitalist economists of the late nineteenth century. This was the essence of economic thought from Jevons to Pigou<sup>1</sup> in Britain, of Böhm-Bawerk to Wieser in Europe, of the generation of J. B. Clark and Carver in America.

Now no one could allege that the views of this school were without practical significance. *If* it was true that existing money offers did express human needs, and that existing money costs did express real sacrifices, then clearly the present economic system (if unalloyed) was perfect. It produced the highest conceivable ratio of satisfactions to sacrifices; the maximum of utility for the minimum of disutility; the greatest wealth for the least "illth"—phrase it how you will. In this epoch capitalist economic science was still essentially normative. It did not hesitate, that is to say, to answer questions involving the word "ought" as well as questions involving the word "is." Capitalism *was* perfect, and therefore it *ought* not to be interfered with in any respect. No economic system has had, in a word, more lusty champions than capitalism found in the persons of the economists of the latter half of the nineteenth century.

The reader may have experienced an increasing sense of uneasiness as we recalled to him the nature of marginal utility theory. He may have felt that it is to-day almost impossible to accept its main conclusions, *viz.*, that money offers on the market are an expression of the relative urgency of human needs.

For example, in 1933 the Rolls Royce Company of Derby, England, was able to report a record year. The demand for its motor-cars had markedly increased. These vehicles are priced at anything from £1,500 to £2,500. In 1933, also, a sharp controversy developed between the British Ministry of Health and the Council of the British Medical Association as to the exact sum of money necessary to purchase sufficient food to maintain the human body in health. The Ministry of Health claimed that

<sup>1</sup> Many capitalist economists, notably Professor Pigou, have guarded themselves by saying that money offers on the market are only a true expression of human needs if substantial economic equality exists. Having, however, made this little acknowledgment to the facts of the real world, they all go on with their argument on the assumption that money offers do to-day express human needs.

a quantity of food values which could be purchased at that time for a sum fluctuating around 5s. 1½d. would keep one person in health for a week. The British Medical Association maintained, on the contrary, that food values which could not be purchased for less than 5s. 10½d. were necessary. The controversy arose in connection with the scale of relief given to the British unemployed, of whom there were between two and two and a half million (plus, say, another five or six million dependants) at that period. After a good deal of learned controversy between the rival authorities,<sup>1</sup> investigations were set on foot to ascertain what sum of money the unemployed actually spent on food per week. This investigation could only be undertaken by the method of sampling. One of the most careful investigations was undertaken by the Medical Officer of Health for the town of Sunderland. It was found that the average cost of the food purchased per week by 36 unemployed families was 3s. 2d. per week per person. (*Annual Report of the Sunderland Medical Officer of Health*, p. 120 *et seq.*) It transpired, then, that the average unemployed family in a typical distressed area spent 1s. 11½d. per week per person less on food than either authority supposed adequate for maintaining human life.

It may be objected that Sunderland is not a fair sample of British conditions. It can be shown, however, that even in the most prosperous areas, and even amongst the fully employed workers, there is a lack of basic and essential food. The following figures are taken from a report made by Mr. Terence Young for the Pilgrims Trust and on behalf of the Becontree Survey Committee. They relate to conditions on the great London County Council Becontree housing estate in April 1932. At this time Becontree had one of the lowest percentages of unemployment of any area in Great Britain (11.1 per cent as against 21.4 per cent as the national average). It appears, however, that some families of employed workers have to apply to the local authorities for free milk, etc. The report gives the following particulars of five such families, the circumstances of which were investigated:

<sup>1</sup> The controversy ended in a reconciliation. But this reconciliation was in effect an admission by the Ministry of Health of the British Medical Association's figure. For it turned out that in the Ministry's figure no allowance for the inevitable wastage of food values involved in handling, packing, and cooking had been made.

## Case A.

	£	s.	d.
Wage earner, employed by H.M. Office of Works, per week	2	3	5
Rent and rates (14s. 1d.) and fares (7s. 7d.)	1	1	8
For all other expenses including food	1	1	9
Family of man, wife, and five children (11, 10, 8, 4, 2)			
"B.M.A." (British Medical Association) scale for food alone £1 11 0			

## Case B.

	£	s.	d.
Wage earner, Post Office cleaner, per week	2	9	6
Rent and rates (14s. 10d.) and fares (6s. 2d.) and furniture instalments (10s.)	1	11	0
For all other expenses, including food	18	6	
Family of man, wife, and six children (11, 9, 7, 5, 3, 1)			
"B.M.A." scale for food alone . £1 12 10			

## Case C.

	£	s.	d.
Wage earner, labourer in motor industry, per week	2	7	8
Rent and rates (18s. 11d.) and fares (1s.)	19	11	
For all other expenses including food	1	7	9
Family of man, wife, and six children (12, 8, 6, 3, 1, 3 weeks)			
"B.M.A." scale for food alone . £1 10 0			

	£	s.	d.
Wage earner, in motor industry, per week	2	6	0
Rent and rates	19	1	
For all other expenses including food	1	6	11
Family of man, wife and seven children (13, 11, 7, 5, 3, 2, 3 months)			
"B.M.A." scale for food alone . £1 16 8			

## Case E.

	£	s.	d.
Wage earner, fitter, employed half-time, unemployed benefit half-time, average per week	2	5	7
Rent and rates (18s. 9d.) fares half week (4s. 6d.)	1	3	3
For all other expenses including food	1	2	4
Family of man, wife, and four children (12, 10, 6, 1)			
"B.M.A." scale for food alone . £1 7 2			

In Poplar, an area about midway between Sunderland and Becontree in its level of unemployment, Dr. Knight has, in 1934, carried out an investigation of the conditions of a relatively large number of unemployed families, and found that five out of every six of the families investigated can spend less money on food than will produce the minimum quantity necessary to sustain healthy life, according to the British Medical Association. (See the *News Chronicle*, Nov. 6th, 1934, and the reports of the Committee Against Malnutrition.)

These three examples, the first chosen from amongst the unemployed workers in a distressed area, the second chosen from amongst employed workers in a prosperous area, the third from unemployed workers in an average area, will perhaps be sufficient (they could be multiplied indefinitely) to demonstrate the single point that in 1932 and 1933 Rolls Royces were rising on consumers' demand schedules as expressed in current money offers, while milk, margarine, potatoes, butter, eggs, meat, bread, and other necessities occupied so low a place in the demand schedules of very many millions of British consumers that they did not expend enough money upon them to maintain healthy life.

The whole *rationale* of marginal utility economics depends, however, upon it being possible to believe that this situation of Rolls Royces relative to necessities of life upon the demand schedules of British consumers in 1933 represented perfectly the relative capacity of these two kinds of commodities to provide satisfactions for human needs. It is necessary to suppose, if the subjective theory of value and the "efforts and sacrifices" theory of costs are to be maintained, that the rising demand for Rolls Royces, and the minimal demand for necessities, represented the free, voluntary, and unfettered choice of the respective consumers of these commodities. It is necessary to these theories to be able to believe that the millions of unemployed workers did not buy enough food to maintain themselves and their families in health because they did not consider that the effort necessary to produce commodities to exchange for further food was worth their while, and that the ladies and gentlemen who bought the extra Rolls Royces caused our available productive resources to be used in such a way as to maximize the

"net satisfaction" of the whole community. It is necessary to be able to believe that to have produced more food and fewer Rolls Royces would have been a senseless interference with people's spontaneous choice of commodities: that such an interference with the market would have reduced the system's capacity to satisfy human needs.

The above is, of course, merely an example of a more general difficulty. How is it possible in the face of observable conditions to believe in those theories of marginal utility economics which demonstrate the inevitability of maximum net satisfactions for all arising from the existing economic system? All around us we see an ever growing demand for the more extreme type of luxuries. Commodities which minister to the most unlikely whims which a human being can entertain are in growing demand. The beauty culture, motor yacht building, luxury motor, luxury hotel industries, etc., etc., enjoy a relative expansion and prosperity. The production of necessities shrinks. Is this because the demand for necessities has been satisfied, so that we are now free to devote a greater and greater proportion of our energies to the provision of luxuries?<sup>1</sup>

In Great Britain to-day it is estimated that seven and a half million people live in vilely overcrowded conditions.<sup>2</sup> Some two to three million persons, with their dependants, are unemployed, and, as we have seen, a substantial, though unknown, percentage of them are undernourished. Mr. O. R. Hobson, the well-known writer on economic and financial subjects, gives some interesting figures in this connection. Writing in *Lloyds Bank Monthly Review* for July 1934 he gives the following figures as a refutation of Mr. Elliot's "root assumption that productivity is threatening to outstrip the desire to consume."

"The National Income of Great Britain and Northern Ireland is estimated at about £3,400,000,000, equivalent to £74

<sup>1</sup> The present British Minister for Agriculture, Mr. Walter Elliot, takes the view that this is so. Everyone, he recently assured us, has now a superabundance of all necessary commodities. The only question is now one of organizing leisure. Mr. Elliot takes this view because of his inability to find a demand for agricultural products. Nobody will buy the food being produced, so, obviously, he feels convinced, they must all have enough of it.

<sup>2</sup> See Mr. Philip Massey's investigation of housing conditions in the *Architects Journal* during 1933.

per head of the population, a figure which does not suggest that the danger of inconveniently large production is very imminent. But of this £3,400,000,000, about £2,550,000,000 represents income belonging to income tax payers—for this is the amount of 'actual income' assessed to income tax in 1932-3, and the 'actual income' figure of the Commissioners of Inland Revenue has been shown by Professor Bowley and Sir Josiah Stamp to be very close to that part of the 'National Income which accrues to the income tax paying class.' Thus the aggregate income of the class below the income tax exemption limit (£100 assessable income, equivalent to £125 earned income) was, say, £850,000,000. Now the total number of income tax payers in 1932-3 was 3,500,000, and if we assume that each of these has, on the average, two-and-a-half dependants, we arrive at the figure of 12,250,000 as the number of persons in the 'income tax paying class.' Subtraction from the total population of 46,000,000 therefore gives the number of persons whose incomes are below the exemption limit as 33,750,000. Dividing this last figure into the residual income of £850,000,000, we have a figure of approximately £25 as the average annual income per capita of the non-income tax paying classes. Would Mr. Elliot seriously claim that there is here evidence that production is so much in excess of consumption that less time ought to be devoted to work and more time allowed for leisure? In order to raise the £25 per annum per head to £3 a week per head—not inherently an extravagant figure for present leisure time spending—a national income well over double the present figure would be necessary."

In other words, an average British working-class family (and this, of course, means that something like half the workers' families in Britain have an income below this amount) has to-day an income of some £25 a year per head. For a family of four this gives an income of £100 a year, or £2 a week. This is the state of things which Mr. Elliot and most contemporary economists call "a glut" of commodities. To deal with this "glut" they demand every sort of measure for the restriction of production. One cannot help wondering whether they would be quite so

anxious to decrease the production of commodities if they themselves were restricted to the annual supply of commodities represented at current prices by £2 a week for a family of four. Mr. Elliot is married, but has no children. So in his case, in order for him to live on the average standard of life of the thirty-three million British non-income tax payers, his income would be £50 a year.

The United States of America does not collect reliable or comprehensive statistics of the standard of living of its inhabitants. Mr. Stuart Chase, in the book which we have already discussed, has, however, collected some.<sup>1</sup> They should be consulted. He recounts this incident :

“ Early in 1933 seven negroes were killed, seven wounded, and one flogged. All were locomotive firemen in the employ of the Illinois Central Railway, operating in Mississippi. They were ambushed while at work, killed, wounded, and flogged by white men for their jobs. White firemen had been replaced in the interests of economy.”

In our decade, therefore, in the richest country in the world, men are killing and wounding each other for the right to receive, in return for peculiarly exhausting toil, a sufficient supply of commodities to maintain their lives. These contemporary facts increase the difficulties involved in believing that existing money offers express human needs.

The difficulties involved in believing in the Marshallian theory of real costs are similar. Can we bring ourselves to believe that the sacrifices undergone by, for example, Lord Rothermere in investing his fortune (some forty million pounds) instead of spending it all at once, is expressed by the sum of money annually paid to him in interest ? Let us suppose that Lord Rothermere's money earns him on an average 5 per cent. In that case it has been found necessary to pay him two million pounds a year in order to induce him to “ wait,” as Marshall would have put it. He is paid this £2 millions because this is the minimum amount that will induce him not to spend his capital of forty million pounds immediately. Two million pounds, then, measures

<sup>1</sup> *The Economy of Abundance*. See also *Seeds of Revolt* by Mauritz A. Hallgeren, especially upon the question of American destitution before the 1929 crisis.

the quantity of pain suffered by Lord Rothermere in not immediately buying forty million pounds' worth of food, clothing, motor-cars, houses, yachts and the like. This sum is necessary in order to induce him to lend his money to production and content himself with an income of two million pounds a year. Similarly we have to believe that the hundred pounds a year given to many British miners for working at the coal face for eight hours a day all the year round is an exact expression of the quantity of effort or pain felt by them in so doing. Thus we must conclude that the pain suffered by Lord Rothermere in waiting is just forty thousand times as great as the pain suffered by the miner in working.

The discrepancies between the view of the world presented to us by the marginal utility economists and by life, are noticeable. The act of faith required in supposing that existing money offers represent human needs is difficult of accomplishment. The Catholic Church only requires of its faithful a belief in the Virgin birth, the infallibility of the Pope (when speaking *ex cathedra*), in a few more dogmas, and in the usual miracles. These are light tasks of faith compared to those imposed on us by the marginal utility economists.

#### SUMMARY OF CHAPTER X

A new school of capitalist economists arises with Senior. It rejects the labour theory of value as unable to account for profits. Capital also said to create value. Capital considered as the result of abstinence. Marshall perfects the conception. "Real costs" as a "supply of efforts and waitings." How are we to add up "efforts and waitings"? Sacrifices as the unifying concept. This theory of real costs the counterpart of the subjective theory of value. Money seen as the measure of disinclination. Its (alleged) infallibility. This theory of real costs the complete justification of capitalism. Sacrifice, unpleasantness, disutility minimized. The system shown to be inherently and absolutely perfect if not interfered with. The subjective theory of value discussed. Value determined by demand. The consumers' "demand schedule." The pleasure-pain ratio as the determinant of value. Psychical quantities.



A commodity's capacity to satisfy human need said to be measured by the amount of money people offer for it. The infallibility of effective demand as an expression of what people really want. The identification of money offers on the market with human needs. The central economic theorem of the heyday of capitalism. The perfection of capitalism again demonstrated.

Present day difficulties of believing in this theorem. Rolls Royces rise and food falls on the British consumers' demand schedules. Undernourishment in Britain and America. Mr. Walter Elliot's view that everybody's demand for commodities has now been satisfied. His consequent policy as British Minister of Agriculture designed to restrict production. Figures as to the average income of most British consumers. Computed by Mr. O. R. Hobson at £25 a head a year for two-thirds of the British population. Speculation as to the effect on Mr. Elliot's economic opinions of a restriction of Mr. and Mrs. Elliot's income to the average income of two-thirds of the British consumers, *viz.*, to £25 per annum each. Difficulty of the conception of real costs as sacrifices. Lord Rothermere's sacrifices in waiting computed to be forty thousand times as great as a typical miner's sacrifices in working. A comparison of the tasks of faith set by the marginal utility economists and by the Catholic Church.

## CHAPTER X

### *The Gelded Science*

If the reader has been feeling the strain of believing in theories which reached conclusions so remarkable as those exhibited in the last chapter, so, as a matter of fact, did many marginal utility economists themselves. Alfred Marshall himself was uneasy.<sup>1</sup> And as time wore on it did not become any easier to maintain that hearty faith in the perfection of the system which had been possible for most of the capitalist economists of the latter part of the nineteenth century.

A new note began to creep in. Professor Pigou, Marshall's best disciple and the father of present day Cambridge economics, devoted much of the ingenuity of his mind to pointing out exceptions to the law that maximum net satisfactions were obtainable by allowing the existing economic system to function in all its purity. Professor Cannan of London (and others) made a more important point. He pointed out that marginal utility theory demonstrated that universal net satisfaction or utility was maximized by the gentle and perpetual movements of supply price just offsetting movements in demand. More of any commodity was demanded and supplied until the point was reached when the demand was nearing satisfaction and the supply was becoming more costly. The rising price just struck the balance at the margin. This involved the idea that commodities yielded a gradually diminishing utility or satisfaction as the amount of them increased. One box of chocolates is delicious, two boxes are nice but rich, three boxes are a mouthful, four boxes of chocolates are too much of a good thing.

Professor Cannan now suggested that the same principle held good of incomes. Was it not true that with every increment of, say, £100 a year in a man's income, his increment of utility, of net satisfaction, became smaller? The difference in satisfaction in having an income of £200 a year instead of £100 a year is enormous. It means (at 1934 British prices) the difference between an adequate and an inadequate supply of necessities. The higher income will just provide health, decency, life itself

<sup>1</sup> See Mr. J. M. Keynes' interesting essay in *Memorials to Alfred Marshall*.

to a small family : the lower will not. The difference between an income of £200 and £300 a year is still very great. So, though a little less so, is the difference between £300 and £400. Each of these increments will give a family access to hitherto inaccessible possibilities of education, medical attention, recreation, a little local travel, etc., etc. The difference between £400 and £500 a year is still considerable, but it is much smaller than the original difference between £100 and £200. Now, to cut a long story short, compare these differences with the difference between an income of £20,100 a year and one of £20,000 a year. This latter difference is relatively negligible. Very well then, said Professor Cannan, it is clear that the net satisfaction of the community as a whole will be increased if incomes are more equitably distributed, provided that total production is not seriously reduced by the redistributory process. For instance, in the case of taxation, it will be "economic," in the sense of tending to maximize satisfactions, to put an extra £100 a year of taxation on the man with the £20,000 income instead of on the man with, say, the £500 a year income.

We notice at once that this theory involves comparing one man's real income (as opposed to his money income) with another's and saying which of them is the greater.<sup>1</sup> It involves saying which income provides, that is to say, its recipient with the greater amount of net satisfaction or utility. The other thing to notice about Professor Cannan's proposition is, however, its significance as a signal of distress from the marginal utility economists who were carrying the strain of trying to connect their theoretical construction with the world around them. It expressed their effort to go on believing that, if existing money offers on the market simply could not any longer be identified with human needs, yet, if appropriate reforms were enacted, if heavy taxation were placed on the rich, for example, they might be brought back into some sort of relation to them. This was certainly a sad change from the confident note of the

<sup>1</sup> We mean by the term "comparing real income" comparing the aggregate of commodities which one man can buy with his income, with the aggregate of commodities which another man can buy with his income, instead of merely comparing the two sums of money. We mean in more familiar, if less exact, language comparing the purchasing power of the two incomes. In just the same way we have spoken of real wages as opposed to money wages. The point is more fully discussed below on p. 157.

earlier marginal utility economists. At the end of the nineteenth century Professor J. B. Clark could still assure himself and his readers that "a natural law exists" which causes "free competition (to tend) to give to labour what labour creates, to capital what capital creates and to entrepreneurs what the co-ordinating function creates." Those days of solid complacency were over. Moreover, the tendency towards a less outrageous distribution of income for which Professor Cannan and his disciples looked, did not eventuate. In spite of the imposition (in Britain) of relatively high taxation upon the rich, some far more powerful force seemed to be at work piling up wealth at one end of the social scale and removing it from the other. It became more and more apparent that some more vigorous revision of economic theory had become imperative if a total rupture between it and the observed facts of life was to be avoided. Somehow or other, the whole *corpus* of marginal utility theory, at once massive and intricate, had to be rescued from the appalling plight into which it had drifted.

A band of rescuers appeared. Professors Cassel, Pareto and Wieser, Mr. Wicksteed and others began to expound marginal utility theory in a new way and with a new emphasis. It was not, however, at once apparent how important were the changes which they were making.

Indeed, it is only to-day, and largely as a result of the more explicit pronouncements of their disciples, such as Professor Robbins, that we see that they have effected a change in capitalist economic thought comparable, in many respects, to that which occurred after the eclipse of Ricardo and the classical school. For what, as we shall see, this change amounts to is the abandonment of the attempt to identify money offers with human needs and money costs with real sacrifices.<sup>1</sup> The reader

<sup>1</sup> There has been a good deal of controversy as to whether the change introduced by this new school is one of form or one of substance. Many Marxist critics (including Mr. Dobb) have taken the view that the change was an exclusively formal one; that the tacit identification of money offers and human needs was still made, but now even less explicitly than before. I have preferred to take the new equilibrium economists at their word when they tell us that they have made a profound change in their science and to show, from their own formulations, what a cloud cuckoo land they have, as a consequence, got themselves into. The point is this: either money offers are still identified explicitly or implicitly with human needs, in which case the distinction between the new equilibrium economists and the older marginal utility theorists is a merely terminological one:

will agree that if it can be established that this step has, on their own confession, been taken by the latest school of capitalist economists, a strong light will be thrown on the character and limitations of contemporary capitalist economic science. Hence it is essential to follow the capitalist economists into the curious fantasy world which they have now created as their "universe of discourse." For we shall find that while they have, admittedly, been able to extricate themselves from the fatal *impasse* into which marginal utility theory had got itself, they have only done so at the cost of a decisive retreat from reality.

It is this retreat which has made it finally impossible for capitalist economics as such even to recognize the existence of crisis: it is this retreat which drives the professors to take to the bypath of monetary theory whenever they are forced by the facts to give consideration to crisis. The remarkable admission that their science can tell us nothing about men's real needs or their satisfactions has been made, however, in anything but an explicit manner. Indeed, it has only been made at all in the roundabout form of denying that it is possible to compare one man's real needs and their satisfaction, or his sacrifices and their compensations, with another's. It has only been made by maintaining that, as real needs and their satisfactions are for ever unascertainable, existing money offers are all that we need concern ourselves with. For the question of the connection of these offers with men's for ever unknowable real needs can never even arise.

It is necessary to show both how twentieth-century capitalist economics has arrived at this conclusion and the consequences of its adoption. In order to do so, we return to the key question of costs. A clear-cut difference between contemporary "equilibrium economics," as this new school is often called, and the older form of marginal utility theory arises over the question of costs.

Contemporary capitalist economists have now almost all abandoned the Marshallian theory of real costs. For this we can hardly blame them. As we have found, Marshall's attempt to

or the connection between money offers and human needs has been repudiated, in which case all the bizarre consequences described in this chapter necessarily follow....

add up the sacrifices involved by one man waiting and another man working, and then to believe that the money presently paid to capitalists and workers for these activities (if waiting is an activity) measured their respective sacrifices, led to the most bizarre conclusions. This theory made the factor common to all commodities, which alone allowed us to add them up and compare them, a psychical quantity, *viz.*, the amount of unpleasantness which their production had necessitated. This was a tenuous basis upon which to rear the whole structure of economic thought. Still it was a basis of a kind.

But what theory of costs have present day capitalist economists substituted for Marshall's doctrine? They have evolved "the theory of displaced alternatives." As its name implies, this view finds a measure for the cost of a commodity in the alternative commodities which might have been produced had the same factors of production been differently employed. This is often called "Wieser's Law." Professor Robbins has defined this theory in the March 1934 number of the *Economic Journal*. He writes: "The conception of costs in modern economic theory is a conception of displaced alternatives: the cost of obtaining anything is what must be surrendered in order to get it. The process of valuation is essentially a process of choice, and costs are the negative aspect of this process. In the theory of exchange, therefore, costs reflect the value of the things surrendered. In the theory of production they reflect also the value of alternative uses of productive factors—that is, of products which do not come into existence because existing products are preferred."

The consequences of the adoption of this elegant and ingenious theory of costs are not always realized, even by contemporary economists. Yet this theorem is at the very basis of contemporary economic thinking in the capitalist world.<sup>1</sup> It is vital to realize, then, that the theory of costs as displaced alternatives is in effect a kind of economic theory of relativity. It escapes from the difficulties of finding any common factor in commodities, by means of which they may be added up and compared, by

<sup>1</sup> Professor Robbins says that Wieser's successors "have brought home to us all its central importance as a unifying principle in the structure of modern analysis" (*Economic Journal*).

*denying that there is any need to add them up or compare them.*

This startling conclusion emerges from an issue discussed in Professor Robbins' article in the *Economic Journal* for March 1934. If we are to measure the cost of the commodities which we *have* produced by the other commodities which we have had to forgo for the sake of the production of the first commodities, we must have some way of measuring the forgone commodities. Professor Knight had suggested that these forgone commodities might be measured by units of physical volume ; so many yards of cotton cloth forgone ; so many tons of coal forgone ; so many hours of opera singing forgone ; so many hours of medical attention forgone ; or what you will. Professor Robbins objects, I think conclusively, to this. We must add up, and then measure, he asserts, the values or costs of the forgone commodities, not their physical quantities, in order to get a significant total.

“ The price which the entrepreneur pays for the factors of production he uses is determined not by the *number* of products which they can produce elsewhere, but by the value of such products. Indeed it is most highly improbable that he knows at all the number of products which can be produced elsewhere. All that he knows are values of the factors of production, which are, of course, reflections of the value of other products. If we reflect upon the way in which equilibrium is established, it is surely obvious that it is only through regard for cost in the value sense that any harmony between technical displacements and prices can be conceived to come about. I conclude that the conception of costs as quantities of goods forgone is not acceptable.”

We cannot doubt but that Professor Robbins is in the right of the matter. You cannot possibly calculate the cost of making motor-cars by finding out the number of locomotives, plus the number of sewing machines, plus the number of steel girders, plus the number of marine engines, which we have had to forgo for the motor-cars' sake. For you cannot add up locomotives, sewing machines, steel girders and marine engines. You can only add up the cost or value of the locomotives, sewing machines, steel girders and marine engines. We are back at our old point.

There must be some factor common to the forgone commodities which you can add up. You must add up their value. And what is their value? The theory of costs as displaced alternatives does not, then, seem to have got us out of the need for a common factor by which commodities may be measured.

We find, however, that contemporary capitalist economists are not perturbed by this consideration. For there is an obvious way out of the difficulty. Why not reckon up the forgone commodities by their price or money cost? Thus the cost of the motor-cars is the £100,000 worth of locomotives, sewing machines, steel girders, etc., forgone.

But just now we showed that no one considered that money constituted the common factor in commodities. In what way, then, if we must not measure quantities of commodities directly in terms of money, does it help us to measure, in terms of money, the commodities which have been forgone for the sake of the production of the first commodities? We begin to see that to call the theory of costs as displaced alternatives an economic theory of relativity is no idle analogy. If the cost of one commodity is measured by the cost of another (and forgone) commodity, there is, it is quite true, no need for any common factor by means of which commodities are rendered commensurable. But then, also, we get no insight into the nature of cost. Cost becomes a quantity which can only be measured by another cost. Cost can only be measured by itself. Now this form of auto-measurement will give only relative results. By means of its use it will still be possible to say that commodity A is dearer than commodity B. But it will be quite without significance to say that commodity A is dear or cheap.

We can satisfy ourselves that contemporary equilibrium economists, when they say that costs can only be measured by the values of the forgone commodities, mean that costs can only be measured by costs, by the completeness with which they accept this necessary corollary; namely, that in future economic quantities cannot have an absolute, but only a relative, significance. Professor Robbins is very explicit on this point. (He makes the point, it is true, in connection with price. But cost is, in this sense, only a special case of price.) And of prices Professor Robbins writes, "Any given price has significance only in relation to



the other prices prevailing at that time. Taken by itself it means nothing." (*The Nature and Significance of Economic Science*.) But if costs and prices have only relative meanings is it not impossible to add them up? We shall find that Professor Robbins fully agrees that this is impossible. This, the impossibility of aggregating commodities, the impossibility of making any totals, necessarily follows from the abandonment of the attempt to find a common factor of commensurability. Moreover, as it is impossible to make up aggregates of commodities at all, it is, *a fortiori*, impossible to compare aggregates of commodities. The one thing which can still be compared is the position of one single commodity on a consumers' demand schedule with the position of another commodity on the same schedule.

These conclusions are inevitably associated with the theory of costs as displaced alternatives. But since they are of the highest importance, we will cite Professor Robbins again in order to show that the best exponents of that theory themselves fully admit them. Professor Robbins, indeed, exhibits the consequences of this theory of costs, and of the subjective theory of value of which it is part, in the widest possible manner. He shows that its adoption makes it impossible to conceive of the category of quantity or magnitude in economics at all. Nothing economic can in future be large or small, valuable or valueless, good or ill, but only larger or smaller, more or less valuable, better or worse. He writes :

"It follows from this that the term which, for the sake of continuity and to raise certain definite associations, we have used hitherto in this chapter, the term 'economic quantity' is really very misleading. A price, it is true, expresses the quantity of money which it is necessary to give in exchange for a given commodity. But its significance is the relationship between this quantity of money and other similar quantities. And the valuations which the price system expresses are not quantities at all. They are arrangements in a certain order. To assume that the scale of relative prices measures any quantity at all save quantities of money is gratuitous metaphysics. Value is a relation, not a measurement." (*The Nature and Significance of Economic Science*, pp. 55-6.)

That is very explicit. But its full implications may not be at once apparent. For example, this view makes it impossible to speak about the total volume of production. For to do so would, of course, imply that it was possible to add up all the commodities produced and make some sort of intelligible total. And this, we are told, is impossible, for commodities have no absolute cost or value. "Value is a relation, not a measurement." There is no "more fundamental something" of which commodities are all composed and in quantities of which they can all be expressed. It is only possible to arrange them in a scale, hierarchy, or order, as they are preferred by consumers expressing their preferences in money offers.

Professor Robbins himself draws this inescapable conclusion.

"Now, as we have seen already, the idea of changes in the total volume of production has no precise content. We may, if we please, attach certain conventional values to certain indices and say that we *define* a change in production as a change in this index; for certain purposes this may be advisable. But there is no analytical justification for this procedure. It does not follow from our conception of an economic good. The kind of empirical generalization which may be made concerning what causes will affect production in this sense, can never achieve the status of a law. For a law must relate to definite conceptions and relationships; and a change in the aggregate of production is not a definite conception." (*The Nature and Significance of Economic Science*, p. 66.)

(We shall make a note of the fact that, although Professor Robbins believes that there is no such thing as the total of production, yet he believes that "for certain purposes" it is advisable to pretend that this quantity exists and to reckon with it.)

The consequences of this conclusion for the question of costs are surprising enough. Let us recall the problem of gross, as compared to net, product. If it is impossible to add up commodities, how are we to take that aggregate of commodities which has been used up in production from that aggregate which has been produced? When there are no aggregates, it is impossible

to take one aggregate from another. Yet it was only by striking this balance, by applying to the complexities of modern production the analogy of the harvest corn minus the seed corn, that the economists were able to put their science upon a rational basis. If they cannot strike this balance, they can hardly refute Major Douglas.<sup>1</sup>

Moreover, the question of costs is, we were forced to admit by the difficulties into which we got in Part I, at the very heart of economics. Marshall's theory of real costs as a supply of "efforts and waitings" was admittedly grotesque. But it did, in the concept of sacrifices, offer some sort of a single factor in quantities of which commodities could be added up and compared. Have not contemporary capitalist economists, in discarding it, lost the last shred of rational basis for their science?

There are, however, still more startling consequences of the adoption of what Professor Robbins well calls the doctrine of "the relativity of economic quantities." This doctrine not only makes it impossible to add up or compare commodities; *it also makes it impossible to compare the magnitude of different people's incomes.* And again it is Professor Robbins himself who not only admits, but strongly urges, this necessary deduction. For what, after all, is an income? It is not just an annually received sum of money—as every recipient of an income fixed at a certain sum of money learns to his cost when there is a general rise in prices. An income is an annual supply of commodities of a certain size. For example, if you have an income of, say, £500 a year, it means that you are able to procure for your use a certain supply, or aggregate, of commodities each year. Now, if I in the same year have an income of £1,000, it means that I am provided with an aggregate, or supply, of commodities of double that size. Is it not, then, possible to say that my real income is double the size of yours? No, it is not, declare Professor Robbins and his school. For to do so would be, it is apparent, to compare the magnitudes of aggregates of commodities. And that, we have been told, is impossible.

<sup>1</sup> This is quite a serious point. It is easy enough to point out the inconsistencies and curiosities of Major Douglas' views. But in order to refute them satisfactorily, so that no sense of doubt remains in the mind, one must go down to basic economic conceptions such as cost and value, as we began to find in Chapter II. Indeed, it is not too much to say that until we have re-established a rational basis for economics a really comprehensive refutation of Douglasism is impossible.

Reflection will show that this inability to compare the incomes of different people and to say which is the larger is an inevitable consequence of the subjective theory of value itself. For what are commodities? They are, as we have agreed from the outset, things which satisfy material or psychical wants.<sup>1</sup> They are "net satisfactions," "utilities," "goods." Does, then, an income of £500 a year supply you with half the quantity of net satisfaction with which an income of £1,000 a year supplies me? This is not necessarily the case at all, we are informed. You may not work as hard as I. You may have a much happier temperament than I. My luxuries may prove but snares and delusions. Who but a metaphysician will care to say which of us enjoys the greater net satisfactions? Indeed, the whole weight of theological opinion is in favour of the view that the poor, or, to use the language of economics, "those in the lower income ranges," enjoy greater net satisfactions than the rich.

Thus the inescapable conclusion of contemporary capitalist economic theory is that it is quite impossible to say that one man's income is larger than any other's. For obviously we must consider their real incomes, not their money incomes, their real supply of commodities or net satisfactions, not their money names. And it is impossible to compare net satisfactions for different persons. The view, which seemed so plausible at first sight, that it was possible to say that a man with an income of £20 a week was ten times richer than a man with an income of £2 a week is, we are assured, quite without foundation.

Thus we find that it is quite impossible to say that anyone is richer than anyone else. Once again, owing to the great practical importance of this conclusion, it is necessary to establish that it really is the position taken up by the more consistent capitalist economists of to-day.<sup>2</sup>

We have already noticed the application of marginal utility

<sup>1</sup> *Vide* Marx's famous definition of a commodity on the first page of Vol. I of *Capital*. "A commodity is primarily an external object, a thing whose qualities enable it, in one way or another, to satisfy human wants. The nature of these wants, whether for instance they arise in the stomach or in the imagination, does not affect the matter."

<sup>2</sup> Naturally there are plenty of capitalist economists who avoid committing themselves to these extravagances. But they do so by the simple means of failing even to attempt to establish any consistent or rational basis for their thought at all. Compared to their shameless eclecticism, the extremities into which Professor Robbins and his school are driven are intellectually respectable.

theory to the question of the distribution of income made by Professor Cannan and the older school. These authorities supposed, we saw, that the utility, or sum of net satisfactions, enjoyed by the community would be increased by an equalitarian redistribution of income, so long as this redistribution did not diminish total production. This proposition Professor Robbins denies. "The proposition we are examining," he writes of it, "begs the great metaphysical question of the scientific comparability of different individual experiences" (*ibid.*, p. 121). And so, to be sure, it does. Professor Cannan and his friends, Professor Robbins has no difficulty in showing, were working on the tacit assumption that it was possible to say that Jones with £10,000 a year was better off than the unemployed miner Smith with £75 a year. Professor Cannan, and most of us, might have supposed that this assumption had, at any rate, a certain sturdy common sense about it. Not at all, Professor Robbins tells us. It is a piece of airy metaphysics. This assumption of the comparability of the incomes of different individuals cannot be made. Professor Robbins elucidates this conclusion as follows: he contrasts the possibility of ranking particular commodities on the same consumers' demand schedule with the impossibility of comparing the magnitude of the aggregate of commodities received as income by one individual with the magnitude of the aggregate received as income by another individual.

"Suppose that a difference of opinion were to arise about A's preferences. Suppose that I thought that, at certain prices, he preferred  $n$  to  $m$ , and you thought that, at the same prices, he preferred  $m$  to  $n$ . It would be easy to settle our differences in a purely scientific manner. Either we could ask A to tell us. Or, if we refused to believe that introspection on A's part was possible, we could expose him to the stimuli in question and observe his behaviour. Either test would be such as to provide the basis for a settlement of the difference of opinion.

"But suppose that we differed about the satisfaction derived by A from an income of £1,000, and the satisfaction derived by B from an income of twice that magnitude. Asking them would provide no solution. Supposing they differed, A might urge that he had more satisfaction than B at the

margin. While B might urge that, on the contrary, he had more satisfaction than A. We do not need to be slavish behaviourists to realize that here is no scientific evidence. *There is no means of testing A's satisfaction as compared with B's.* If we tested the state of their blood-streams, that would be a test of blood, not satisfaction. Introspection does not enable A to discover what is going on in B's mind, nor B to discover what is going on in A's. There is no way of comparing the satisfactions of different people " (*ibid.*, pp. 123-4).

"There is no way of comparing the satisfactions" (that is, the real incomes) "of different people."—This is the final dictum of contemporary capitalist economic thought. The larger part of the population of the globe is denied an adequate supply of the necessaries of life. Very many millions are permanently undernourished. A few tens of thousands, on the other hand, command a supply of commodities, the range, variety, and costliness of which are quite unparalleled in human history. Is it possible to form a view as to which of these two groups of persons enjoy the greater satisfactions? It is utterly, absolutely impossible to do so, our theorists tell us, with noticeable emphasis. It would be sheer metaphysics to suppose that it was more satisfactory to be able to buy ten dinners than a quarter of a dinner. To come to any conclusion on the point would be to betray the scientific character of economic thought. Now there is little doubt that to compare the real incomes of different people in the modern world would be to betray *something*. We can guess this by the extraordinary emphasis with which we are forbidden to do so. But would the thing betrayed be the scientific integrity of economic thought? Is there not just a possibility that it would be something of more immediate importance, to wit, our existing social order, which would be betrayed, if ever the admission was made that it was better to have a full belly than an empty one?

The practical significance of this view may be further elucidated by reflecting upon the dictum of one of Professor Robbins' German-speaking colleagues, Dr. Haberler. Professor Robbins translates this dictum as follows:

"Science is guilty of trespassing beyond its necessary limits—that is to say, it is delivering a judgment of value—if it

attempts to lay down for others which of two real incomes is the 'larger.' To decide on this, to decide which real income is to be preferred, is a task which can only be done by him who is to enjoy it—that is, by the individual as 'economic subject' " (*ibid.*, p. 63, footnote).

The mind's eye detects the doctor contemplating in turn the incomes of Herr Thyssen and of a man in a Nazi Labour Camp drawing three marks a week. After prolonged reflection Dr. Haberler turns sadly and modestly away with the report that he is quite unable to decide which of these two is the richer. What scientific scruples, and, above all, what tact! We cannot help feeling how extraordinarily convenient these scruples must be for the good doctor. In a world which rocks and reels because of an unparalleled inequality in the distribution of wealth, how soothing to have come to the conclusion that the magnitudes of wealth enjoyed by different individuals cannot be compared at all.

This is the condition of complete, if convenient, impotence to which equilibrium economics has been reduced by the abandonment of the attempt to find a factor common to commodities which will render them commensurable: by the abandonment, that is to say, of any objective theory of value. The final step was taken when the second generation of marginal utility economists fled from the sinking ship of Marshall's real costs, when they abandoned, that is to say, the impossible attempt to identify money offers with human needs. For the necessity of abandoning this attempt is the whole *raison d'être* of contemporary "equilibrium theory." No economist in his senses would have taken up the extraordinary position that it was impossible to compare different people's incomes, for example, unless this was the one remaining way of saving the whole structure of marginal utility theory. Professor Robbins and his colleagues have not confined themselves within the curious fantasy world of the doctrine of the relativity of economic quantities because, as they imply, of their scientific scruples. They have done so because by this decisive retreat from reality alone could the basic theorems of their science be saved.

With the declaration of the relativity of economic quantities  
Lc

the last possibility of adding up commodities to form aggregates ; of comparing these aggregates ; of conceiving of gross as compared to net production ; of conceiving of a total of production at all ; or of comparing individual incomes, was lost. Equilibrium economics, its professors themselves demonstrate, can do none of these things. What then, may we ask, can it do ? Do not its professors feel their impotence ? The poet has assured us that,

*Nuns fret not at their convent's narrow room ;  
And hermits are contented with their cells ;*

while the poet himself found it

*pastime to be bound  
Within the sonnet's scanty plot of ground.*<sup>1</sup>

In the same way, equilibrium economists may be content within the confines of their simultaneous equations. Yet how narrow those confines are we can now realize. Professor Robbins himself describes them as follows :

“ The pure theory of equilibrium enables us to understand how, given the valuations of the various economic subjects and the facts of the legal and technical environment, a system of relationships can be conceived towards which existing relationships may be regarded as tending. It enables us to describe that distribution of resources which, given the valuations of the individuals concerned, satisfies demand most fully ” (*ibid.*, p. 127).

Once again we must remember that these “ valuations of the various economic subjects ” are the existing money offers on the market, and that we are forbidden, on pain of becoming metaphysical, to enquire even what relation these money offers have to human need. Hence all that modern capitalist economics even claims to tell us is what the effect on prices will be if the money offers for this commodity decline and for that commodity increase, if the supply of that commodity increases or of this

<sup>1</sup> Wordsworth, “ The Sonnet-Prison.”



commodity declines. In the complexity of the modern market this question may itself become complex, and may require a system of simultaneous equations for its solution. But this solution is all that contemporary capitalist economics can even attempt to give us.

The truth is that in emptying out the unquestionably muddy bath water of the Marshallian theory of real costs the equilibrium economists have, whether they realize it or not, emptied out of their science the baby of significance also. Political Economy, in the hands of the masters of the classical school, was a virile science. It provided conclusions intensely important for action. Contemporary capitalist economics, on the contrary, is an impotent, a gelled science, unable to form any opinions whatsoever upon the issues which chiefly concern us.

#### SUMMARY OF CHAPTER X

Strain of preserving their faith felt by marginal utility economists. Professor Pigou's exceptions. Professor Cannan's theory of the diminishing marginal utility of incomes. His equalitarian proposals seen as a distress signal. Failure of redistributory taxation to restore a connection between money offers on the market and human needs. Necessity of rescuing the *corpus* of marginal utility theory. The rescuers appear. The new school of equilibrium economists. They cut the painter between human needs and money offers. They abandon all attempt to add up commodities. This emerges from their theory of costs as displaced alternatives. An economic theory of relativity. Costs are now measured by costs. Consequent relativity of economic quantities. Widest possible application of this view given by Professor Robbins. There is no such thing as an economic quantity. "Value is a relation, not a measurement." Hence impossibility of conceiving of a total of production. Impossibility of taking commodities used up in production from commodities produced.

The final consequence of the theory of relativity of economic quantities is an inability to compare the incomes of different people. Full acceptance of this conclusion by Professor Robbins.

Professor Cannan's equalitarian proposal arraigned as "gratuitous metaphysics." Emphatic prohibition of the attempt to say whether one man is better off than another. Dr. Haberler's scruples. Dr. Haberler's tact. This total impotence a result of the abandonment of an objective theory of value. Do equilibrium economists fret within their equations' "scanty plot of ground"? The baby of significance thrown out with the bath water of real costs. The gelded science.

# PART III

## THE LABOUR THEORY OF VALUE

“If the labour theory of value be used to understand the movement of history and make revolutions, the price theory can be used to understand the movement of stocks and to make money.”

*(J. D. Bernal from an unpublished work.)*



## CHAPTER XI

### *The Function of a Theory of Value*

IN previous chapters we have traced how during the last hundred years a creeping paralysis has pervaded every limb of capitalist economics, until to-day total impotence has overcome the science. Nor is there any room for doubt as to how the disease began. We traced it to its source in the abandonment of an objective standard of value.

We must, then, re-examine the ground upon which the labour theory of value was rejected. For this seems to have been the point at which the science took the wrong turning. We saw in Chapter X that the labour theory of value was rejected because of its inability, in the form in which it was then enunciated, to account for the phenomenon of profit. It was Marx who discovered the solution to this problem. Before, however, describing his solution it will be well to expose some of the popular misconceptions of why the labour theory of value, even in its pre-Marxian form, was rejected.

Now the labour theory of value was not rejected, as the popularizers of modern capitalist economic theory sometimes ignorantly allege, because the classical economists neglected the fact that labour might be misdirected : that they supposed that a hundred hours expended in digging a purposeless hole in the ground created more value than ten hours spent in producing corn. Ricardo, who was a man of genius (to say nothing of some of the greatest intellects of the eighteenth century from Quesnay to Adam Smith), was not likely to be in need of correction upon such a point from the authors of Victorian textbooks. The classical economists all pointed out, of course, that when they spoke of labour creating value, they meant what Marx called "socially necessary labour" : labour, that is to say, devoted to creating commodities which supplied human needs.

Moreover, the phrase "misdirected labour" does not cover alone such activities as digging holes in the ground and filling them up again. It covers cases of producing more of a useful commodity than society needs. If the world needs 100 million bushels of wheat and its farmers produce 150 million bushels,

some of their labour was not socially necessary and did not, therefore, create value. Again, if one of the farmers has been a poor workman and manager and has used up twice as many hours of labour time in producing 100 bushels as the others, this does not mean that he has produced twice as much value. For his labours were not socially necessary. He has, by mismanagement, worked unnecessarily.<sup>1</sup>

Already we catch sight of the essential nature of the theory. For if only that labour which turns out to have been well directed counts as socially necessary, and therefore value-producing, labour, then it is clear that the labour theory of value will not enable you to foretell prices, and can never have been intended to do so. For you cannot tell which labour was socially necessary until after the commodity has been sold. The character of the labour, the degree to which it was socially necessary or not, is revealed by the price at which the commodity is sold. It is the movement of prices which reveals the character of the labour. Is it not immediately apparent that the function for which the labour theory of value was elaborated was to bring into man's consciousness what it was that the fluctuations of price revealed?

The function of the theory was to enable men to comprehend that what, for example, the danger sign of a falling price of wheat was trying to signal to the farmers was that the labour which they were putting into the planting and cultivating of further acres was not socially necessary labour; that the community already had all the wheat it wanted, and that men should apply their available hours of labour time to producing something else.

It is true that the movement of prices will in the end compel the obedience of the producers without men having any comprehension of what is happening. The farmers will be ruined if they go on devoting their labour to producing more wheat, even though they have never grasped the fact that the cause of their ruin is that their labour has ceased to be socially necessary, and so has ceased to produce value. Gradually, painfully, the farmers will be driven to devote their labour to producing something other than wheat. But the classical economists believed

<sup>1</sup> These points are discussed exhaustively in chapter iii of *Capital*, Vol. I.

that it was of the utmost importance that men should consciously realize that this was the underlying reality which manifested itself in the movement of prices. They believed that mankind could never comprehend their economic life until they had brought this process into their consciousness; and that the labour theory of value, and the labour theory of value alone, enabled them to do this.<sup>1</sup>

Nor was the labour theory of value rejected by the capitalist economists of the last hundred years because it was impossible to foretell the *price* at which a particular commodity would sell by knowing the amount of money which had been spent upon paying labour for its production. For neither Ricardo nor any classical economist had ever claimed that the labour theory of value explained the market *price* at which commodities were sold. What they had claimed was that the labour theory of value explained the market *value* of commodities. This distinction between market price and market value is worth elucidation. For the latter day "refutations" of the labour theory of value actually confound the two. The everyday "refutation" of the labour theory of value alleges that the amount of labour necessary to the production of a commodity cannot determine its value because we find that as often as not the sum of money paid out in wages during the course of the production of a commodity bears little or no relation to the price which that commodity fetches.

Now, whatever defects the theory had, even in the form in which Ricardo used it, it was not open to this objection. Ricardo was perfectly aware that the price realized by a commodity on the market fluctuated with supply and demand. But, he said, there must be some central point round about which these fluctuations occur. There must, in particular, be a lower limit below which the price of a commodity cannot go, for more than a short period, however large the potential supply may be,

<sup>1</sup> The distinction between Marx on the one hand, and Ricardo and the classical economists on the other, on this point is that Ricardo considered that the market did provide us with a rational, if automatic, control of the process of exchanging the products of our labour. Marx, on the contrary, saw that the control provided by the market was leading to more and more irrational results. Hence he saw in the labour theory of value the proof of the necessity of instituting a conscious control of economic life other than the market. And this difference of interpretation followed, as we shall see immediately, from the establishment by Marx of the distinction between labour and labour power.

and however limited the demand. For, if the price goes below a certain point it will make the production of any supply of the commodity unprofitable. Hence, if this commodity is to exist at all, it has to have a certain minimum price which is not determined by supply and demand. Supply and demand cannot be the sole determinants of price.

Again, Ricardo suggested, let us suppose that supply and demand are equal; that they are "in equilibrium," what in these circumstances will determine price? It cannot be supply and demand, for they will exert equal and opposite pulls and must cancel out. The equality of supply and demand will determine the stability of the price, will prevent, that is to say, the price from either rising or falling. But what will determine the particular level at which the price will remain stable? There must be some other factor at work. The play of supply and demand is a very adequate explanation of the fluctuations of price. But it is no explanation at all of what it is that fluctuates. Demand and supply account for how much the price of any particular commodity will deviate from the average. But what determines the average price of commodities? There must be something which market prices express by means of their very fluctuations: some level which the constant see-saw of supply and demand is determining as an average. This level Ricardo and the classical school called *market value*. And market value, this central average of market prices, this point round which market prices fluctuated, was, they said, determined by the amount of labour necessary to the production of commodities. Thus from the outset the labour theory of value was quite inapplicable to the problem of trying to predict what market prices would be. Even in the simplest conditions of production, the fact that six hours of labour paid at 6*d.* per hour, had been used in the production of a commodity would not tell you that the price of that commodity would be 36*d.* All that it would tell you was that 36*d.* was the market *value* of that commodity, that 36*d.* was the level around which the opposing pulls of supply and demand would cause the market price to fluctuate, if the commodity was to be produced at all.

Thus the labour theory of value never claimed to be able to predict the prices at which particular commodities would sell on



particular occasions. A knowledge of it would not help a farmer, or a merchant, or an artisan to make money. For it is precisely the fluctuations of price which interest those who have to sell on the market. But the classical economists claimed that their theorem did, and did alone, enable us to understand what it was that we were doing when we bought and sold commodities. We were exchanging the products of our labours, and the ratios at which these products exchanged was determined in the long run by nothing but the amount of labour which had been necessary to their production.

Nor was the labour theory of value rejected because of any difficulty in accounting for the greater amount of value which was, clearly, imparted to a commodity by an hour of skilled as against an hour of unskilled labour. In the hypothetical society of individual, independent producers, which was the unconscious background of the minds of the classical economists, it was easy enough to see that an hour of the skilled labour of, say, a cobbler would count as, say, an hour and a quarter of the labour of a worker with no training. For the hours spent on the training of the cobbler were also being paid for. Thus the fact that the market showed that the products of skilled labour sold for more, in proportion to the number of hours of work which had been put into them, than the products of unskilled labour, appeared merely to confirm the validity of the theory.<sup>1</sup>

We can now understand what it was that the classical economists claimed for their theorem. The utility of the labour theory of value was not that it would enable us to predict prices and so help us to make money. *The utility of the labour theory of value was, we repeat, that it enabled us to bring into consciousness what we were unconsciously and instinctively doing when we bought and sold our products.* The classical economists believed that their basic theorem was the key to an understanding of the

<sup>1</sup> The misconceptions as to the nature of the labour theory of value are endless, but we might notice one more, and a simple one. It is sometimes said that labour cannot be the sole source of value, because commodities are produced in differing natural conditions—some wheat on fertile land and some on infertile, etc., etc. Yet they all sell at the same price in the same market. Hence the fertility of the land must have contributed to the value of the wheat. It should be, but is not, needless to say that Smith, Ricardo and the other classical economists were always careful to point out that they spoke of commodities produced in average conditions. An owner-cultivator of more than averagely fertile land possessed a natural monopoly which enabled him to sell his wheat at above its value.

economic life of society *as a whole*. They did not think that it provided a full analysis of the motives which induced people to part with a particular commodity at a particular price and no other. But they did believe that it provided an essential analysis of what would be the total result of the actions of all the dealers on a free market when each of them was following his own economic interest. Their theory, they believed, provided a law which governed the results which would flow from setting up a free market and exchanging commodities upon it. They believed, to use one of their expressions which has been much (and hastily) sneered at, that there was "an unseen hand" which determined what would be the net result of the self-seeking, competitive activities of a large number of free and independent dealers upon the market. A general net result, which had been wished by none, but which yet was determinate and predictable, would flow, they believed, from the innumerable and competitive transactions of the market.

There were, moreover, immediately practical and political deductions to be made from the theory. If hours of labour embodied in commodities were, in fact, what we bought and sold, then, clearly, he who had not laboured should have nothing to sell, and consequently should be unable to buy. At the end of the eighteenth century there was obviously one class in the community which was able to buy freely and yet could never be detected to be labouring or to be selling any products of its labour. There were the landlords. Nor did the classical economists hesitate to draw the conclusion that everybody else would be so much the richer if they all ceased to give the landlords the products of many hours of their own labour without receiving any products of the landlords' labour in return.

We see that, although the labour theory of value was never able, and never claimed to be able, to tell you anything about what price you would get for your commodity, no matter how much labour you had put into it, it did tell you a great deal about how the total of commodities produced was divided up between different classes in the community, and how, by very obvious implication, it ought to be divided up. It showed you with precision that what you were really doing, for example

when you paid your landlord his rent, was to surrender to him so many hours of your working time. It stripped away the thick mystification with which the labyrinthine system of exchanges had covered the old feudal relationships. It revealed that there was no essential difference between working for nothing, as did the serf, for, say, one day a week on the domain of the overlord, and paying the squire one-seventh of your annual income in rent. In either case you were surrendering the products of one-seventh of your labour time to an individual who surrendered no products of his labour time to you in return.

Nor were the classical economists at a loss to explain how it was that the landlords were able to force the rest of the community to surrender a substantial proportion of the products of its labour to them, without the landlords giving any equivalent products in return. The landlords were enabled to extract this tribute because they possessed a monopoly of one of the indispensable factors necessary to production, namely, the land. Moreover, the land was an indispensable factor of production of which there was a naturally and absolutely limited supply. There were in each community so many cultivable acres of land, and no more. Therefore any body of persons who could acquire and retain possession of the land acquired a natural monopoly by means of which they could force the rest of the community to pay them tribute. For they could deny to any producer the possibility of production by denying him the use of the land.

We have already seen the nature of the difficulty which wrecked the labour theory of value in its pre-Marxian form. The characteristic form of the organization of production ceased to be that of small, independent, individual producers for the market employing no one but themselves and became that of employers of labour, paying wages to a group of workers, and consequently owning all the products made in their factories, or on their farms. A new class of persons appeared called either capitalists or employers, and deriving an income, which they calculated as a percentage on their capital, from the difference between what they paid out to their workers by way of wages and what they received in money for their

products. A new economic category had appeared, namely, profit.

Moreover, this new class of capitalist employers, and consequently this category, profit, on which they lived, became of greater and greater importance. Not only did the production of commodities by independent, individual workers, selling the product of their labour directly on the market, become more and more the exception, and production by a group of workers, working for wages paid by an employer, become more and more the rule. Distinct from this process, but associated with it, the actual technical methods of production also began to change. Commodities were decreasingly produced by the direct application of simple labour, using a few hand tools, to raw materials. More and more commodities began to be produced by a long, complex, and in many cases mechanized process. Industry was becoming, for the first time, technically developed. It was beginning to use, that is to say, more and more capital in proportion to labour. In the middle of the eighteenth century, let us say,<sup>1</sup> 100,000 yards of cotton cloth was produced by 10,000 workers using £1,000 worth of capital in the form of simple spindles, hand looms and the like. In the eighteen-thirties 100,000 yards of cloth were produced by 100 workers using £10,000 worth of capital in the form of huge power driven looms and spindles : in the form of the mills of Lancashire, in fact.

It was found by observation that this change had done something strange to market value. It seemed increasingly impossible any longer to maintain that the market value of commodities, the level, that is to say, round which their market prices might be observed to be fluctuating, corresponded to the amount of labour which had gone to their production. It was, after all, easy enough to test the thing out. Given a stable level of wages, the amount of money paid out in wages told you the number of hours of labour which had gone to the production of a commodity. If workers were paid 1s. an hour and the wages bill was twenty shillings, twenty hours of labour had gone to the production of the commodity. Twenty shillings should then be the market value of the commodity, the level round which its market price should fluctuate. But it didn't. Not only was the average price of the commodity observed to exceed this level, and so realize a profit

<sup>1</sup> Needless to say, the figures are wholly hypothetical.

on his capital for its capitalist producer. But also the commodities produced by the new technically developed methods did not seem to fall in value in proportion to the diminution of labour embodied in them. For if the above simple calculation had been true, the commodities which were being produced by the new, mechanized forms of production should have fallen in market value to an enormous extent. If formerly it had taken 1,000 hours of labour at 1s. an hour to make a commodity and now it took only 100, this commodity's market value should have fallen from 1,000 to 100 shillings. But, in fact, it was found that, though the market value of a commodity subject to the new labour saving technique did fall, it did not seem to fall nearly as much as this.

For, it was observed, although the new methods of production economized labour, they only did so by using more capital. You could only produce the same commodity with one-tenth of the number of man-hours of work by using, let us say, five times as much capital as before. What, then, was more natural than to connect these facts and to conclude that the capital as well as the labour necessary to the production of a commodity created value? Not only was it natural to say this. There was a pressing and practical reason for saying it. If it could be shown that capital played its part in producing value, so then also did the capitalist. He played his part by abstentions, by "waitings," by savings. Even if he never went near the factory, his was just as necessary a part in the creation of value as was the workers'. Accordingly, it was just as deserving of reward. And this as we saw is exactly what the post-classical capitalist economists from Senior onwards did say.

This, then, was the rock which sank the classical school. Their labour theory of value was unable to account for the emergence of the category profit at all. And as time went on this category of profit became of greater and greater importance. The margin between the labour costs of a commodity and its average selling price became greater and greater. For the part played in its production by human labour became smaller, and the part played by capital resources became greater. It became more and more impossible to say that the labourer in a highly mechanized factory was selling his labour embodied in that

factory's products ; for the amount which he and his fellow workers received in wages bore less and less relation to the amount received for the product. This, it was felt, was fatal to the labour theory of value. And certainly as production became more and more "capitalistic," it did become more and more difficult to maintain that the amount of labour needed to produce a particular commodity determined the average price at which that commodity was sold.<sup>1</sup> Gradually the capitalist economists abandoned the labour theory of value. In its place they adopted, as we have seen, the subjective theory of value, combined for the first seventy-five years or so with a theory of real costs based on Senior's "abstinence," or Marshall's "efforts and waitings," and combined to-day with the theory of costs as displaced alternatives.

We have already described, using largely the words of contemporary capitalist economists themselves, the truly pitiable condition to which economic thought has been reduced as a result of this process. The capitalist economists have become, unless they break their own rules, impotent even to consider the crises of the system which they purport to explain. Moreover, we saw that this final condition of prostration is a direct result of having abandoned all attempts to find any common factor which could make commodities commensurable : of having abandoned the attempt to find a tenable, objective theory of value. For, though the capitalist economists decided that labour could no longer be the sole source of value, they were never, as we saw, able to discover any other objective, unifying principle upon which to base their science.

Hence it is certainly no idle task to re-examine the labour theory of value and decide whether its abandonment was indeed necessary. If it was, then, as the reader will perhaps agree, it will be better to abandon economic discourse altogether. For we have discovered that a theory of value alone enables us to add up and compare commodities. And, unless we can do that, significant economic discourse becomes impossible.

<sup>1</sup> It is curious to reflect on what evolution Ricardo's views would have undergone if it had not been for his early death. Would he, too, have abandoned the labour theory of value and become an eclectic, or would he have become a Marxist? It is almost impossible to envisage either eventuality. It almost seems that his premature death in 1823 was a theoretical necessity!

What, then, was Marx's solution of the problem? Marx concentrated his attention on that change in the organization of production which created the problem. He emphasized strongly the emergence of a new character in the drama of production. He concentrated his gaze on the entry of this new character, unknown (or known in an embryonic form alone) to previous ages, namely, the capitalist employer of labour.

It was as if the original independent peasant or artisan producer had been split up into two separate persons who now each performed one of his two functions. For the self-employing peasant, or artisan, had actually made the commodity with his own hands, and, as its owner, had taken it to market and sold it. But now the making was done by a wage worker and the owning, and consequently taking to market, was done by a capitalist employer. And the capitalist employer was observed to be able to obtain on the market more than he paid out to his wage workers. How could it be said, then, that all that was sold on the market was the labour of the wage workers embodied in the product? For we knew the price of these workers' labour. It was the amount of their wages. But the price which the capitalist employer got on the market for the commodity habitually exceeded this amount. Was it not clear, then, that some element other than labour had gone to the determination of the commodity's habitual price, or value?

It was not, said Marx. For the argument as stated above contained a hidden fallacy. The typical wage worker did not now sell his labour embodied in a product. He did not sell any of the previously existing commodities; he sold a new commodity. He sold his ability or capacity to work. A new commodity, Marx declared, had made its appearance upon the market. For the sale by a worker of his ability to work, to a capitalist employer, was a new transaction, differing in kind from the sale of a commodity made by an independent worker. Take the case of an artisan baker who bakes a loaf of bread and sells his labour embodied in it to his customer. The customer wants this bread for his own consumption and must previously have sold some commodity or service, embodying his labour, in order to have got the money with which to pay the baker.

Compare this transaction with that effected when a wage earning bakery worker sells, say, twelve hours of his working time to a master baker. The master baker does not want the bread which this wage worker will bake. He is only getting it baked in order later on to sell it. Is it not clear that the wage earning bakery worker is not selling his labour in at all the same sense as did the independent artisan baker when he sold his labour, embodied in a loaf? As we saw, the classical economists, when they spoke of men exchanging their labours, had always envisaged this latter kind of transaction, in which an independent worker or artisan had been able, since he could get hold of the necessary means of production, to make a saleable embodiment of his labour.

It was a confusion of thought, Marx declared, to apply this conception to the wholly new conditions which had grown up. For in these new conditions the mass of mankind could not sell their labour; for they could not get hold of the necessary "means of production," without which they could perform no labour. Landless agricultural workers, or artisans for whom it was impossible to acquire the indispensable means of production, could not possibly sell their labour. For before you could sell your labour, in the sense in which the classical economists had always used that phrase, you had to perform it. You had to do the job before you could have a saleable product which could appear on the market as the embodiment of your labour. And workers who had lost their access to the means of production could not do any job. All they could do was to sell their *ability to labour*, their *potential* power to create commodities, to someone who had possession of the means of production. For this latent ability to labour, this potential power to work, could only become actual kinetic labour when it was united with the indispensable means of production. And this could only be done by someone who owned these means of production. Hence, Marx insisted, it was essential, if hopeless confusion was to be avoided, to coin some new term to describe this new commodity which a wage worker sold to a capitalist employer when he entered into a wage contract with that employer. For he did not sell the capitalist his labour. On the contrary, the wage worker was unable to labour until he had been brought by the capitalist into contact with



the means of production. All he could sell to the capitalist was his potential power to labour, or, as Marx called it, his *labour power*.

If we want practical evidence of the existence of this commodity labour power, as distinct from labour, we need only consider the existence of "overseers." For what is the function of an overseer? It is, is it not, to ensure that the potential labour power which the worker has sold to the capitalist is in fact turned, during the time in which the worker is within the factory gates, into actual, kinetic labour? What function could an overseer have if what the worker sold to the capitalist was his labour, which he had already performed? But the worker cannot sell his labour until he has performed that labour. And he cannot perform any labour until he has been admitted within the factory gates and given access to the means of production. While he is outside in the street bargaining with the capitalist all he has to sell is his potential ability to labour, if and when the factory gates are opened and he is reunited to the means of production. But, for the same reason, all the capitalist has bought is this ability to labour, not the actually completed job. So the capitalist has to take the greatest care that the worker actually does do the job, does translate his *labour power* into actual, completed *labour*.

But what, then, does the capitalist sell when he takes to market the commodity which has been made by the workers during the period in which they, having sold him their labour power, work for him? *He*, the capitalist, then sells his workers' labour. For now that labour has been performed. He puts on to the market an embodiment of those labours. For it was in his workshop, during "his time" (as the revealing phrase runs) that the commodity was made. Thus the real position is that the wage worker sells his labour power to the capitalist, while the capitalist sells the wage workers' labour, embodied in the commodity.

We see at once that this apparently fine distinction between labour and labour power is all important. For if the capitalist, in selling the finished product, and not the worker, in making the wage contract, sells the worker's labour, then this explains how there can be a habitual difference between the price realized by the product and the amount paid to the worker in wages.

It explains, in a word, the appearance of profit. For there is no reason to suppose that the price of the labour power sold by the worker to the capitalist will be the same as the price of the labour, embodied in a commodity, which the capitalist sells on the market. For how, according to the labour theory of value itself, will the value, the average, habitual price, of the labour power be determined? By the amount of labour which has been necessary to the production of this newly introduced commodity, labour power. And the amount of labour necessary to the production of, say, twelve hours of labour power is, clearly, the amount of labour necessary to feed and generally sustain the labourer who performs this twelve hours of work. But the price or value of the labour actually performed by the worker during that period, and so embodied into a commodity, will depend on quite different considerations.

Moreover, it is not difficult to see that the value of the labour power will be habitually less than the value of the labour. For how is it that the workers are now forced to sell their mere ability to work, instead of selling, as they used to, their actually completed labours, embodied in commodities? It is, as we saw, because they have lost their access to the indispensable means of production. These means of production have become the effective monopoly, not, it is true, of any one person, but of the capitalist employers as a class. The whole necessity of the workers to work for an employer, instead of for themselves, has arisen because the indispensable means of production have got out of their possession and into the possession of a different and separate class of persons. Hence in the last analysis it is an ever tightening monopoly of the means of production which enables the capitalist employers to pay the wage workers less than the value of their labour: which enables the employers to pay them no more than the value of their labour power, as determined by the necessity of maintaining these workers' strength and efficiency.

How this effective monopoly of the necessary means of production grew up, how, in other words, the workers lost their access, not only to the land, but, progressively, to all the other means of production as well, forms the subject of the historical chapters of *Capital*. Marx is able to establish that the monopolization of the land by the landlords is merely a special case of the

much wider process of the step by step monopolization of all the necessary means of production by a newly emerging class, namely, the capitalist employers of labour. And it is from this monopoly of the means of production, and not from any mysterious power to create value supposed to be possessed by their capital, that the capitalist employers derive their power to extract profit.<sup>1</sup>

The preceding Part of this book has, it is hoped, helped to bring out the full significance of this difference of opinion as to the source of profit. For it was by supposing that capital produced value that the economists were committed to the extravagance of assuming that Lord Rothermere suffered 40,000 times as much pain in waiting as a miner suffered in working, and to all the rest of the palpable nonsense of modern economics. For, whatever plausibility there may once have been in alleging that a man's abstinence in saving up his capital was tantamount to his working, there is none whatever in suggesting that a modern rentier's dividends come to him as a result of any contribution made by him to the process of production. The truth is that once we abandon the simple rational conception that what matters to us human beings in the process of production is the work which that process directly and indirectly involves, and that consequently human labour is the father of all value, we are bound to set our feet upon a path which leads to a *reductio ad absurdum*. We are bound to find ourselves providing the justification for those monstrosities of co-existing starvation and luxury which we considered in the last chapter. For the elaborate provision of this justification has been the real function of post-classical, or as Marx called it "apologetic," capitalist economics.

It is hardly too much to say that the elucidation of this distinction between labour and labour power, which it is so easy to overlook as a piece of mere terminological hair-splitting, is Marx's primary contribution to economic science. For by it he was able to demonstrate that a capitalist economy was still, in

<sup>1</sup> Of course, we all know the arguments of those capitalist spokesmen who tell us that the workers have not been excluded from access to the means of production: that the capitalist class has no monopoly of the available factors of production: that there is nothing but their own lack of initiative and intelligence which prevents the unemployed workers of the United States Steel Corporation from starting up in the steel producing business on their own, etc., etc., etc. But I cannot bring myself to refute such "arguments."

the final analysis, an exchange of human labour embodied in commodities. But now, he showed, the process of exchange was not carried on between all citizens. It was only carried on between the capitalist producers, who sold the labours of the wage workers, after they had embodied them in commodities. And they were enabled to do this since their monopoly of the means of production had in turn enabled them to purchase slices (measured by time) of the workers' ability to work, of their labour power. The attainment of this distinction by Marx is the watershed of economic science. This is the great divide. For without this distinction it is impossible to reconcile the observed facts with any rational, objective theory of value. On the basis of this distinction, however, it is possible to erect a theoretical structure which will fully account for the real phenomena of present day society.

Even after this vital distinction has been realized, however, it is necessary to remember what is the function of the labour theory of value. Its function is not to predict the prices which particular commodities will fetch. It is, even in the form in which Marx perfected it, largely irrelevant to the day-to-day problems of commercial life. What then is its function? The function of the labour theory of value in its final Marxian form is to allow us to peer below the bewildering kaleidoscope of the market and to see what it is that men are exchanging. It reveals to us what the dealers on the market are doing *collectively*. It is true that they are unconscious that they are doing anything collectively. As good individualists they concentrate their attention exclusively on enriching themselves. But there is no doubt whatsoever that their activities have a collective aspect. The community which they control is either stagnating, prospering, or declining. It is subject to cyclical crises or it is not. There is, evidently, a net result of their competitive activities. And this net result comes about independently of the conscious will of any of them. For the actions of each form too small a part of the whole to exercise any appreciable effect.

Hence there must be, if only we can perceive it, a certain law, or laws, which determine objectively this collective net result of the activities of a society of dealers on, and capitalist producers

for, a free market. These laws can be formulated upon the basis of the labour theory of value. By their use we can tell whether the possibilities of a particular set of social relations are exhausted or not. We can tell, for instance, why our present set of social relations are producing the misery of by far the larger part of the human race. In fine, we can attack those all important problems which modern capitalist economic thought is, on its own confession, strictly debarred from considering. In particular, we shall find that we are at last enabled to deal adequately with the question of cyclical crises. We shall be able to give a convincing and self-consistent account of each phase of the economic cycle of capitalism and shall be able to reach conclusions which have prediction value. We shall be able to see what measures will tend to exacerbate the severity of the crises, what mitigate their effects, and whether or not it is true that the future crises of the system will grow more and more severe.

#### SUMMARY OF CHAPTER XI

Why did the capitalist economists reject the labour theory of value ? For this seems to have been the fatal turning point which led to the present plight of the science. It was not because labour might be misdirected. Ricardo accounted for this. He never claimed that the labour theory of value would enable you to predict the movements of prices. It was not because Ricardo denied that supply and demand determined market prices. Market prices and market values distinguished. It was not because of any difficulty in reducing skilled to unskilled labour.

The theory was rejected, as we saw, because it could give no account of profit. Moreover, as production became more and more technically developed, the element in value apparently created by capital became larger and larger. Plausibility of this objection. Practical advantage of supposing that capital, and consequently the capitalist, creates value, whether he works or not. Need to recollect what the function of the labour theory of value is.

A reminder, however, of what the abandonment of the

labour theory of value led to. What, then, was Marx's solution of the problem?

Marx distinguished between labour and labour power. The independent peasant or artisan sells his labour, embodied in a commodity, on the market. The wage worker sells his labour power to a capitalist employer, who then sells this worker's labour, embodied in the capitalist's commodity.

The difference between labour and labour power established. Labour cannot be sold by workers, who cannot labour because they are excluded from access to the indispensable means of production. All that such workers can sell is their potential ability or power to labour. The overseer as a functionary necessary to the process of ensuring that the worker, whose ability to labour the capitalist has bought, really does labour.

Crucial nature of this apparently terminological distinction. It alone enables us to understand capitalist society as an exchange of labours.

The function of the labour theory of value in its Marxian form. Its function is to enable us to establish the law or laws which govern the historical movement of the capitalist system as a whole. By the use of these laws alone shall we be able to attack our special problem of the nature of the cyclical crises of capitalism.

## CHAPTER XII

### *The Function of a Theory of Value (continued)*

THE most striking proof of the validity of the labour theory of value can be obtained by a pragmatic test. The next Part will adopt, therefore, the labour theory of value, in the form in which Marx perfected it, as a working hypothesis and endeavour to demonstrate its application to the problems of capitalist crisis.

We shall have to spend some space, however, in defining Marx's economic categories. For, unless we do that, his crisis analysis will be incomprehensible. The reader will perhaps bear with this process of acquiring a new set of implements for the prosecution of our enquiry when he recollects how badly our existing set of economic categories broke down when we attempted in Part I to get at the essential nature of capitalism and its crises. Marx takes the whole of the first two volumes of *Capital* for the establishment of these categories. He only applies them to the problem of the analysis of crisis in Vol. III.<sup>1</sup> In the brief space of two chapters we shall be able to define them only—not attempting to establish them. We shall, however, be able to judge of their validity by the amount of assistance which they give us when we come to use them for an attack upon our problem.

Let us first of all clear up some current misconceptions in regard to Marx's formulation of the labour theory of value. Just as it was necessary to dispose of the points which did *not* wreck the labour theory of value in the form used by the classical economists, so now we must define what Marx did *not* mean by the labour theory of value. This procedure is necessitated by the undoubted difficulty with which minds steeped, as all of ours must necessarily be, in the subjective, demand-and-supply, economic thought of the last hundred years, find in approaching any objective theory of value.

We are often told that Marx asserted that "labour was the cause of all value." More precisely, what Marx asserted was that the value of commodities was determined by the amount of

<sup>1</sup> And to a lesser extent in the final section of Vol. II.

socially necessary labour time which had gone to their production. By putting in the words "socially necessary" he was, as we noticed in connection with Ricardo's views, guarding against the ignorant criticism that he supposed that misdirected or misapplied human labour created value. But he most certainly did mean that definite, objective human labour performed either by our hands or by the nerve cells of our brains, was the sole source of value. He meant that the work of living, breathing men and women was the only thing that could add a jot of value to any commodity in the world.

At a first hearing, minds which have been subjected to our type of training rebel against this proposition. How can it be said, we feel, that in modern conditions, with our semi-automatic factories, pouring forth commodities from hundreds of marvellous machines, controlled by only a few overseers, labour is responsible for all the commodities, all the flood of values, produced? Our difficulty reveals that we have not made up our minds as to the meaning of the word "value." We should probably agree that the term "valuable" is associated with the term "expensive." Again we shall agree that "valuable" also means "useful." But we may not have realized that these two meanings are wholly different. Let us return to the example of air. Nothing is more useful than air. We die immediately without it. Yet would you call air valuable? Hardly, because it is not expensive. It is clearly only valuable in one sense of the word. It is only "use valuable."

Now we said that our marvellous semi-automatic machines were pouring forth a flood of values. But are they? We have seen that value and expensiveness certainly have something to do with each other. Now are these marvellous machines rendering the commodities which they produce more or less expensive? Everybody knows that they are making them less expensive. That is their whole point. The "easier," the more automatically, the more prolifically, commodities are produced, the cheaper, not the dearer, they become. So, in this sense of the word, the machines certainly do not seem to be producing value. They are, on the contrary, producing less and less valuable, in the sense of expensive, commodities. They are making the commodities approximate, to some extent, to the condition of air.



They are producing more and more commodities, but less and less valuable commodities.

But stay, you object, the commodities produced by the machines are just as good, just as valuable in the sense of useful, as hand-made ones. How can we say that they are less valuable? It is clear that we are using the word valuable in two different senses. We are using it to mean useful, and we are using it to mean expensive. Now if you mean by valuable useful, then, of course, machines produce value, and neither Marx, nor anyone else outside an asylum, ever denied it. But if you mean by valuable expensive, then is it not equally obvious that machines do not produce value? Machines make things cheaper, not dearer. They make each commodity cheaper, but they make more commodities than a non-mechanical process would have made. Perhaps, then, they make the same amount of value as the non-mechanical process, only spread out thinner over more commodities, as it were? Machines, on this hypothesis, evidently do not create value, they merely spread a given amount of value over more commodities.

But if machines do not create value, what does? It certainly looks as if value is created by human labour alone. (We have already seen, however, that there is an apparent objection to this. The machines make commodities cheaper. But not apparently the whole amount cheaper that they would have to be if the machines added no value of their own. We shall find, however, that this proposition is true of the total production of society taken as a whole.)

Now the classical economists used the two terms "use value" and "exchange value," for valuable in the sense of useful and for valuable in the sense of expensive, respectively. Thus we can say that the object of a productive process ought to be to create the greatest amount of use value for the least amount of exchange value. This means creating more and more commodities with less and less labour. Marx considers what would happen if this process was carried to its logical conclusion. "If," he writes, "the same use-value could be created without labour, it would have no exchange-value, yet it would have the same useful effect as ever." (*Capital*, Vol. III., p. 758.) This makes it perfectly clear that when we say that labour is the

father of all value we mean that it is the father of all "exchange value." If an article can be produced with no labour at all, it will have no exchange value, no "expensiveness," but, naturally, it may be just as useful as ever.<sup>1</sup>

A failure to realize these truths is at the bottom of some painful nonsense now current, more especially in America, as to the growth of semi-automatic production having finally disproved the labour theory of value. The technocrats, and even Mr. Stuart Chase, are apt to tell us delightful stories about factories in New Jersey, or anywhere else, regulated by photo-electric cells, etc., etc., which turn out endless streams of commodities without the touch of a human hand. How then, they ask triumphantly, can we still maintain that labour is the source of all value? They forget, of course, that before we could say that these commodities had been produced without the aid of human labour, the automatic factories would have to build themselves as well as run themselves—to say nothing of the raw materials growing and mining themselves and transporting themselves to the factory.

Let us put aside these practical difficulties, however. For the point at issue is admittedly the tendency. Does the admitted fact (Marxist theory is, incidentally, founded on this fact) that production is being carried on with less and less labour per commodity produced mean that the labour theory of value is becoming less true? We have just seen that Marx himself considered the question of the logical conclusion of this process, namely, perfectly automatic production involving no labour. If one can imagine such a thing, then certainly no exchange value would be created. There would be an infinite, inexhaustible supply of use values, without cost, without price, and without exchange value.

Such a delightful state of things would, of course, be the complete demonstration of the labour theory of value. If only we could achieve perfectly automatic production, then indeed we could show to everyone that it was labour alone which created value. For, once we had eliminated labour, we could supply

<sup>1</sup> Cf. Marx's statement in *The Critique of Political Economy* that "it is wrong to speak of labour as the only source of wealth" (p. 33). Or, again, his remark in *Wage-Labour and Capital* that inventions increase the amount of products but do not necessarily result in "a larger amount of exchange-value."

everybody's wants without price or limit by an infinite supply of perfect, priceless, and valueless goods. Moreover, it is true that modern productive technique is reducing the amount of labour necessary for the production of a given amount of commodities so rapidly that the production of value is being seriously cut down. And this, as we began to guess in Chapter VI, is at the root of the crisis of capitalism.

Poor Marx ! Fifty years ago and more, long before the photo-electric cell was dreamt of, he foresaw the coming of more and more automatic methods of production (or, as he would have put it, of a limitless raising of the productivity of labour). He prophesied the day when we should have "torrents of wealth," when we should be able to satisfy our needs with incomparably less labour than before, when, finally, there would be enough of everything for all. And he founded his view, both of the inevitability of the overthrow of capitalism, and of the possibility of realizing communism, on the coming of this age of plenty.

What has been his reward ? In Marx's own day he was mocked as a visionary. Few indeed could see that the day when "the sources of social wealth should all run more freely," as he put it, would certainly come. There was little realization that the machine was changing the fundamental conditions of human life. To-day these changes are apparent to every journalist. And our journalists tell us that Marx is an out-of-date theorist, whose doctrines apply to an age of scarcity alone ! Not having taken the trouble to read a line of Marx's work, they have no inkling that his analysis foresaw and explained precisely the effects of the revolutionary changes in productive technique which we are now experiencing. Nor have they the slightest comprehension that his analysis alone enables us to understand how to change our social relations in such a way as to make our new powers of production into our servants instead of our devastating masters. Marx must bear the injustice of such ignoramuses as his allotted portion. He will do so the more easily as throughout the world serious men are using the knowledge he has bequeathed to them as the essential instrument of their salvation.

The reader will probably agree, then, that once the term value has been defined there is nothing unreasonable in saying that machines do not create value.

A second misconception may be cleared up by noticing that Marx maintained that the rate of wages which was paid to the workers who produced a commodity did not affect that commodity's value.

That certainly seems odd. If labour is the creator of all value, must not a commodity's average price, or value, depend upon how much money has been paid for the labour which produced it? Will not an increase in wages increase a commodity's value and a decline in wages reduce it? We can see at once that this conclusion is false, however, when we recollect Marx's distinction between labour and labour power. Wages are the price of labour power. Hence a change in the price of labour power can have no effect upon the amount of labour which the use of that labour power embodies in a commodity. We can also look at it in this way. The labour theory of value declares that the amount of work (reckoned in days, hours, and minutes) which is necessary to the making of a commodity is what determines that commodity's value. Now, whether you pay workers 1s. an hour or £1 an hour for making a commodity will not alter the number of hours which they have to work to get the job done. It is the *time* which has to be used up in production, not the *money*, which is the unit of measurement. Reflection will show that this is inevitably so. All presentable theories of value, even all presentable theories of cost, have to get behind the money names. Marshall, we remember, distinguished between "real costs" and "money costs." The real costs were the "efforts and waitings": the sums of money which had to be paid out in order to elicit them were the money costs. In the same way it is the hours of labour themselves which have gone to the production of a commodity which constitute its value. If a capitalist is induced to pay his workers 1s. 3d. an hour instead of 1s. an hour, it will not enable him to sell his commodity any dearer. It will merely, as he will say, "eat into his profits." In other words, what an increase in the rate of wages does is, not to raise the value of a commodity, but to give the workers and the capitalist a different share in that value.<sup>1</sup>

<sup>1</sup> The reader will discover in subsequent chapters that this statement is only true, as it stands, of the total product of a capitalist society.

A third misconception may be dissipated by a remark of Marx's in Vol. I of *Capital*. "The absolute value of the commodity which he produces is, in itself, of no interest to the capitalist." That is worth thinking over. Value, Marx maintained, was wholly and solely created by human labour. Does it follow that the value of a commodity will be limited to the amount of labour which a particular capitalist has employed in creating it? By no means. That would only be true if one particular capitalist produced the commodity in the sense that he mined the coal, to smelt the iron, to make the steel, to fashion the plates, to build the commodity—say, a ship. In practice, he buys half-finished goods—steel plates, in this instance. And these plates have already had a great deal of human labour expended upon them during the time in which they have been fashioned out of, say, iron ore from the mountains above Bilbao and coal from a Lanarkshire pit. Hence they contain a great deal of value. This value the shipbuilding capitalist buys when he buys the steel plates and then sells again when he sells the ship. It is an item on both sides of his account. It is an item of costs and of receipts. Hence it is clear that the size of this item, other things being equal, is indifferent to him. It is, in other words, no more profitable to produce costly commodities than cheap ones. Woolworth makes even more money than Rolls Royce. What matters to particular capitalists is not the absolute value, or, for that matter, the absolute price, of the commodities produced, but the size of the difference between the cost of these commodities and their selling price.

Moreover, we have just shown that one way of reducing the cost of commodities does not affect their value. If a capitalist cuts his workers' wages, he will not lessen the value of the commodities which he produces. For their value is determined by the number of man-hours of work which are necessary to their production. The money paid out per hour does not alter this number. So a capitalist can increase or diminish his profits on a commodity without altering its value at all. This makes us feel the force of the contention that value, as Marx defined it, is a concept in which the capitalists have little interest.

Indeed, ever since Marx formulated his theory of value the capitalists have pointedly expressed their indifference to it. The

very latest of Marx's capitalist biographers, Mr. Carr, remarks, for instance, that "value and surplus value (as defined by Marx) are pure abstractions of thought unrelated to any values which are normally the object of economic investigation."<sup>1</sup> This, as Mr. Carr says, has been the unanimous verdict of the capitalist critics ever since they grasped that Marx really did mean that the value of a particular commodity had no precise relation to its price: that a commodity might sink in value and yet rise both in price and in cost of production, or *vice versa*, and that consequently, for each particular capitalist, changes in the value of a commodity made no defined difference to the profit he might make from that commodity's production.

Having discovered this, the capitalist critics have not ceased to exclaim that they have no further need of witnesses as to the futility of Marx's theories. Marx himself emptied out, they tell us, all significance from his concept. Value, in his sense of the term, is some metaphysical abstraction. It has nothing to do with our very practical problems. With this verdict they return to consider the apparently more practical concepts of cost and of demand and supply. They return to those plausible, but, as we found, profoundly unsatisfactory, economic categories with which we tried to unravel the problem of capitalist crisis in Part I.

It remains to be seen, however, if Marx's concept of value, which certainly is an abstraction, is, or is not, a significant abstraction. Marx maintained that it was possible by the use of this category, value, which was equal neither to the cost nor to the price of a particular commodity, to construct a system of further categories of thought by the aid of which it was in turn possible to discover "the law of motion" of the capitalist system.

"To reveal the economic law of motion of modern society" was, Marx wrote in the preface to *Capital*, "the final purpose" of his book. And it is for this purpose, and for this purpose alone, that the category, value, as defined by him, is significant. Marx, in a word, believed that the labour theory of value would alone enable us to discover the destinies of the capitalist system. This is a problem worthy of attention. If the labour theory of value,

<sup>1</sup> *Karl Marx*, by E. H. Carr. (London, 1934.)

and the categories built upon it, do enable us to understand the nature of the capitalist system and its crises, and hence to make valid predictions about that system's future destinies, then they are some of the most significant abstractions ever achieved by the mind of man.

#### SUMMARY OF CHAPTER XII

The labour theory of value in its Marxian form elucidated by a process of elimination. What Marx did not mean when he said that labour was the creator of all value. Value as use and value as expense. Do machines produce value? Current nonsense about the semi-automatic machine having disproved the labour theory of value. Poor Marx! The ignoramuses.

Marx said that the rate of wages paid in the production of a commodity did not affect that commodity's value. Value is determined by the weeks, hours, and minutes of labour sold, and not by the price of the labour power bought. Absolute value of no interest to the capitalists. Absolute cost of no interest to the capitalists. Difference between cost and price all that interests them. Mr. Carr expresses the capitalists' lack of interest in Marx's category, value. The purpose for which Marx invented this category. "To reveal the economic law of motion of modern society." Are the Marxian categories significant abstractions?

## CHAPTER XIII

### *The Marxian Categories*

THERE is no need, for our immediate purpose, to argue further about Marx's conception of value. For, after all, if Marx likes to define the value of a commodity as the number of hours of socially necessary labour time which have gone to make it, he is at perfect liberty to do so. Once he has made that definition, then, for the purposes of his discourse, that is what value, by definition, is. It remains open to his critics, however, to attempt to show that value so defined is an empty abstraction : that it has no significance : that it explains nothing : that it does not help us to understand the nature of the economic system or to make predictions as to that system's future destiny. And this is what all capitalist economists do attempt to show.

We already know what function it was that Marx claimed for the category, value, defined as socially necessary labour time. He claimed that this concept alone allowed us to understand what it was that we were doing when we produced and exchanged commodities. It alone allowed us to realize that what we were doing was to exchange the products of our labour, and therefore to exchange those hours of our working time which had become embodied in the products.

Now it is clear that, if this concept of value is to have significance, it must be possible to show what is the relationship of prices to the amount of socially necessary labour time embodied in commodities. (Though, as we saw, it is not in the least necessary to the labour theory of value to be able to predict what the price of a particular commodity will be from the amount of labour at a given rate of wages which has been performed upon it.<sup>1</sup> Neither Marx nor Ricardo, for that matter, ever for a moment suggested that the labour theory of value provided a guide to the commodity market.)

It is important to establish this point. For Marx, or rather Marxism, has suffered at the hands of apologetic defenders. A series of recent writers, including Mr. G. D. H. Cole, Professor

<sup>1</sup> As is maintained, for example, by Professor A. D. Lindsay. See *Karl Marx's Capital*, by A. D. Lindsay. The Master of Balliol's plausible, fallacious, and superficial little book served also to mislead Professor Sidney Hook.



Sidney Hook, and Mr. Raymond Postgate, have attempted either to preserve the labour theory of value in an abstract and meaningless form, or to abandon it and yet preserve the conclusions which Marx draws from it. This latter proceeding is like abandoning the ground storey of a house to the destruction of the flames, while hoping that somehow or other the upper storeys may remain suspended unharmed in mid-air. No position could be more unfortunate. Every competent capitalist critic (as, for example, Mr. Carr, Marx's latest English biographer) is able to expose it. The labour theory of value must be abandoned if the relationship between socially necessary labour time and prices cannot be explained. And if the labour theory of value is abandoned, the whole of Marx's gigantic construction crashes to the ground.

The best way of deciding the question of whether the Marxian category value has significance or not, is to see how Marx used both it and the other economic categories which he builds upon it. But in order to do this, we must define what these categories are. We shall no more than enumerate them, with but a very minimum of definition, since the reader can turn at will to Marx's own exhaustive establishment of them in *Capital*.

Surplus value is the first consequential category. *If* value is socially necessary labour time, and nothing else, profit, it can be shown, is nothing but unpaid labour. *If* all value is created by the work of living human beings, then values accruing to persons for reasons other than their work must have been taken from the persons whose work did create them. This is best seen in the case of values received by persons who do no work at all—say, a rentier drawing dividends. Such values must have been created by someone's work. Hence they must have been taken from their creator and given to their recipient. Marx coined the well-known term "surplus value" to define such transferred values. It is, we observe, a much wider term than profit. It covers rent, interest, and profit; it covers, in a word, every kind of value receivable for any reason other than the performance of work.<sup>1</sup>

<sup>1</sup> We felt the need for an inclusive term of this sort in Chapter VI, p. 87, when we had to explain that what Dr. Hayek had to restore, in order to produce an adequate supply of savings, was the profitability of production. For we saw at once that the existence of all types of those high incomes from which savings are chiefly made depended, directly or indirectly, upon production itself being profitable.

Surplus value may, from one point of view, be defined as value received by persons who give no equivalent value in return for it. And it is only if socially necessary labour time, let it be emphasized once more, is the sole source of value, that rent, interest, and profit are values of this character. If, as the capitalist economists maintain, the function of "waiting," which a rentier certainly performs, is also a source of value, then clearly the rentier does give an equivalent for the value which he receives.<sup>1</sup> Nor, from a capitalist point of view, is there anything strained about the hypothesis that waiting, as well as working, is a source of value. It is true that commodities for which we have to wait are in one sense more valuable (in the sense of costly) than commodities which can be produced immediately. But there is, surely, not the slightest doubt that there is a real, fundamental and essential distinction between laborious human activity and the value or cost which its expenditure entails, and any cost or value which can be said to be entailed by waiting. For unless we make this distinction human history becomes incomprehensible. If we confound working and owning, or waiting, which is what capitalist theories of value amount to in the last analysis, and suggest that it costs a man as much to wait for his annual dividends instead of spending his whole capital at once, as it costs a man to work ten hours a day, we flout all human experience, and justify all the murderous monstrosities of the present situation.

It is not, however, within the purpose of these pages to attempt to establish the validity of the economic category, surplus value. What we are doing is merely to define what that category is. Then we shall use it, and the other categories associated with it, for an attack upon our basic problem of what it is that causes capitalist crises. Thus the reader will be able to judge for himself whether the category is an empty and insignificant abstraction, or an extremely fruitful hypothesis which makes the economic life of our times comprehensible.

The way in which this surplus value is transferred from those who produce it by working to those who receive it by waiting, to regress to Marshall's phrase, is the central theme of the first

<sup>1</sup> The rentier waits, as we saw in the case of Lord Rothermere, in the sense that he forbears to spend all his money at once, and instead contents himself with living on his income.

volume of *Capital*. How, Marx enquires in Part 3 of Vol. I, do those who own the means of production get hold of the values which form their incomes? The business was clear enough in the days of slavery. The slave owner simply made the slave work for him and took all the value which the slave produced over and above what was necessary to keep the slave alive. But the modern capitalists and landlords do not own the workers. How is it that they, too, seem to be able to get hold of all the values which the workers produce over and above what the workers need to live on? They do it, as we have seen, because of the peculiar nature of the commodity which the worker sells to the capitalist. The worker sells to the capitalist his ability to work, his "labour power," and sells it by the day, hour, or week. And what is the value of this commodity, labour power, which is itself the father of value? Its value, we repeat, is reckoned, in just the same way as all other commodities. A man's labour power is worth the amount of labour which it has taken to produce it. It is worth, that is to say, the number of hours of labour time which have been used up in producing the food, clothes, training facilities, etc., necessary to keep up a man's ability to work. Thus the value of labour power is a sum which will command the amount of commodities which will keep up the worker's health and strength and enable him to rear up children of equal health, strength and technical ability to replace him.

In this respect labour power is just like any other commodity. But in another respect it is unlike every other commodity. Its value is the amount of labour time which will produce it. But its *use* is that it itself creates value. Just as the use of the commodity called a bed is to sleep on, so the use of the commodity called labour power is to produce value. It is in order to use it for this purpose, and for no other, that the capitalist buys it. Moreover, in present day conditions the use of this commodity, labour power, will produce more value than is paid for it. Put a worker in a modern textile mill and he will produce more shirting per year than he can possibly wear. Indeed, he will produce much more shirting than he can wear, plus an amount which will exchange for the other necessities of life with which he must be provided. But he need only be paid enough to enable him to buy these necessities. Put a worker on a modern farm and he will

produce far more food than he can eat. But he need only be paid enough money to buy the food that he eats plus the clothes that he wears and the other necessities which he must have. In a word, the worker produces more value than he uses up. The difference is surplus value.<sup>1</sup> And this difference the capitalist owns. He has bought the worker's labour power at its proper value. He owes the worker nothing. On the rules of the capitalist system he is fully entitled to the whole product. This is where the capitalist's profit, the rentier's interest, and the landlord's rent, come from.<sup>2</sup>

Marx backs up this argument by repeatedly asking where the values which form the incomes of the capitalists can come from if they do not come from this difference between what the worker is paid and what the worker produces? They cannot come from exchanges between the capitalists. It is quite true that one capitalist can, and often does, "do" another capitalist in the eye. He may get twice as much value as he gives in any particular deal. Is this, then, where the capitalists' incomes come from? Many capitalists think so. But, if you look at the matter from the point of view of the capitalist class as a whole, this cannot be true. Look at it even from the point of view of the two capitalists in the above unequal bargain. One made an income by getting the better of the other. But he only made his income at the expense of the other. What he gained his friend lost. Taking them both together, they still had the same sum of values as before. Swapping values about, no matter whether unequally or equally, cannot add anything to the total. "The capitalist class cannot overreach itself," as Marx puts it in Vol. I of *Capital*.<sup>3</sup>

<sup>1</sup> The reader will notice at once that the concept surplus value is the lineal descendant of the Physiocrats' *produit net*. But the category value, defined as socially necessary labour time, has made it possible to generalize the idea; to apply it to the productive system as a whole, and not merely to the simple, special case of agriculture.

<sup>2</sup> They come, to link the point with the argument of the last chapters, from the difference between the value of the worker's labour power, which the capitalist buys, and the value of the worker's labour, embodied in a commodity, which the capitalist sells. And the capitalist is enabled to make the worker accept the value of his labour power, instead of standing out for the full value of his labour, because the capitalist's ownership of the means of production makes it impossible for the worker to work without the capitalist's consent.

<sup>3</sup> The definitive refutation of the possibility that the capitalists can derive their incomes from swapping values about amongst themselves occurs in Vol. II, pp. 560-70, which contains Marx's onslaught on Destutt de Tracy.

So much for surplus value. The three other essential categories which Marx builds upon the labour theory of value are constant capital, variable capital, and the price of production. It is necessary to an understanding of Marx's construction to get these categories clear.

Above all, it is necessary to distinguish Marx's categories, constant and variable capital, from the familiar capitalist categories of fixed and circulating capital. Now all these categories are different ways of splitting up the total amount of capital which it is necessary to lay out for the production of a given supply of commodities. Let us take the capitalist way first. Let us divide up a block of capital into its fixed and circulating parts. Let us instance the capital necessary to the production of, say, a locomotive. Let us say that £100,000 had to be put down for plant; that £4,900 had to be put down for raw materials, for steel, for coal for generating the power, for the machine oil used up in turning the various parts, for the copper, etc., etc.; and that £1,000 had to be put down for wages in order to pay for, say, 10,000 man-hours of work at 2s. an hour. So £105,900 had to be laid out to make the locomotive.

In order to distinguish the circulating from the fixed part of this sum of capital we must enquire at which price the locomotive must be sold. Will it have to be sold for £105,900 in order to avoid a loss? Of course not. For the £100,000 spent on the plant is not all used up in making this one locomotive. The cost of the locomotive is only the capital which is actually used up in making it. In this case £4,900 for raw materials: £1,000 for labour. Can the locomotive be sold without loss for £5,900 then? Scarcely. For, although the whole £100,000 worth of plant was not used up in making one locomotive, some of it was used up by way of wear and tear. The plant, in other words, will only produce so many locomotives before it is worn out or becomes obsolete, and has to be scrapped. Hence its owners must reckon so much "depreciation," as they will call it, on to the cost of each locomotive produced. Say that it is in this case £100.<sup>1</sup>

<sup>1</sup> All the figures in this example are, of course, quite arbitrary. They are chosen for arithmetical simplicity rather than for technical versimilitude. This can in no way affect the argument which could be (and is by Marx) expressed algebraically in terms of £X and £Y.

So the locomotive cannot be sold without loss for less than £6,000. For it has cost £6,000 to produce. £6,000 of capital has actually been used up in making it. This portion of the capital is called the *circulating capital*. For it circulates with every act of production. It is consumed in producing the locomotive. It only comes back into its owners' hands when the locomotive is sold. The other part of the capital, the plant worth £100,000, is called the *fixed capital*. For this capital is, relatively at any rate, fixed in the hands of its owners. Its value does not circulate with each product. Or, rather, it only circulates piecemeal as, bit by bit, it is worn out and renewed. Such, then, are the categories of fixed and circulating<sup>1</sup> capital.

Before going on to define Marx's categories of constant and variable capital, it will be convenient to elucidate what the actual selling price of the locomotive will be. For this will enable us to define Marx's third category, the price of production. The locomotive can, we saw, be sold without loss for £6,000. But will it be sold for £6,000? Hardly. For in that case there will be "nothing in" the whole business for the owners of the firm of locomotive builders. They are not in business for their health. They are not in business for building locomotives as an end in itself. They are not, and cannot be expected to be, putting up and risking their capital for the altruistic purpose of supplying the community's railway lines with tractive power. They are only building locomotives as a means to an end; and that end is making a profit. If they cannot sell their locomotives at a price high enough to yield them a profit, they will sooner or later cease building them: for the essential motive behind the whole business will have disappeared. Hence our locomotive must be sold at some figure above £6,000. It must show some margin of profit. But how much profit must the locomotive show? How much above £6,000 must its price be in order to induce the firm to continue building locomotives?

The answer, if you think of it, must be that the locomotive must fetch enough above its cost of production to make an average amount of profit for the firm. And by "average" we mean the average amount of profit being made at that time in

Sometimes referred to as "working capital."

that community by capital invested in all kinds of business.<sup>1</sup> Moreover, although this is not apparent at first sight, locomotives really are sold in the long run at this figure. They are sold at their cost of production plus a sum which gives the capitalists who have made them an average rate of profit on their capital. This seems peculiar. For we cannot imagine the firm of locomotive builders pricing its products in this way. The firm will try to get just as high a price as possible. Why should it modestly limit itself to the average rate of profit? On the other hand, there may be a slump in locomotives. The locomotive building firm may not be able to get a price which will yield the average rate of profit. It seems as if, far from the price always being such as to yield an average rate of profit on the capital invested, it will never be fixed at this sum. For in one state of the market the firm will not limit itself to this price and in the other it will not be able to get this price.

And yet, as the general average, this will be the price charged. For what will happen if the locomotive firm charges such high prices that it makes above the average rate of profit on its capital? Why, other capitalists will go into the locomotive building business. They will see that locomotive building is "a good thing." New capital, new competitors, will be attracted into the industry. And these new competitors will charge a price which gives them no more than the average rate of profit on their capital, and will therefore take the custom from the old firm. But what will happen if it is impossible to get even a price which is high enough to yield an average rate of profit? Why, then the capitalists who produce locomotives will be continually impelled to transfer their capital to other fields. No doubt they will have difficulty in doing so. But yet gradually the amount of capital invested in the locomotive building industry will be reduced. Works will not be repaired or kept up to date. Inefficient works will be scrapped. Gradually the amount of capital invested in this branch of production will be reduced until the

<sup>1</sup> Allowing, also, of course, for the element of risk. The rate of profit obtainable in lines of production exposed to exceptional risks of, for instance, climatic disturbance, will be higher than in lines not so exposed. But in the long run the rate of profit obtained by firms in these risky employments will turn out to be the same as the others. For their higher rate of profit will be compensated for by the fact that some of them will lose their capital altogether.

point is reached when what remains will again be able to earn the average rate of profit. (For the output of locomotives will have gone down until the price which can be got for them goes up to the necessary figure.) In either case, then, the price which our firm will charge for locomotives will actually be, in the long run average, what we said, *viz.*, its cost of production plus a sum which will yield an average rate of profit on the capital invested. For deviations from this price in either direction will be corrected by the attraction or repulsion of capital to or from the industry.

Thus the prices charged for commodities must be such as will result in an even average rate of profit being made throughout the productive system. Must they indeed, the reader may be objecting? How can it possibly be said that all capitalist firms make a uniform average rate of profit? What nonsense! Why you have only to look into the newspapers to see that some firms are making huge profits while others are making huge losses; that, in fact, no two firms ever seem to make the same rate of profit.

Here we begin to appreciate how very different the phenomena of the capitalist world appear according to the angle from which you look at them. These ceaseless fluctuations of the profits made by different firms undeniably exist. But these are the fluctuations by which that even, average rate of profit is struck. These fluctuations exercise those continual pulls and pushes which shift capital about from one line of production to another in obedience to the shifting pull of effective demand. Moreover, these fluctuations have to be fairly sharp; the pulls and pushes which they exercise have to be fairly strong, for the transfer of capital from one line of production to another is a rather difficult business. You cannot easily or quickly switch over your locomotive building plant to the production of motor omnibuses. Indeed, in this case you probably cannot do it at all. You will have to scrap your existing plant, write off its capital value, and begin building a 'bus-building plant afresh. Hence it is obvious that the price of 'buses must be, and must remain for quite a long time, at a point which will give an amount of profit substantially above the average; and that the price of locomotives must fall, and stay down, to a point which will give a profit substantially below the average, before the transfer of capital



will occur. But all this does not alter the fact that this transfer does, and must, occur in the end : that any exceptionally high rate of profit must be gradually evened down by the crowd of competitors who will come into this line of business, anxious to be "in on a good thing," and that any exceptionally low rate of profit must in the end be evened up by the emigration of capital from this line of business.<sup>1</sup>

To return, however, to our example. Let us say that in the case of our locomotive costing £6,000 to build, a selling price of £7,000 will give the firm the average rate of profit on its capital. Now what will that rate be ? Will it be a profit of £1,000 on the £6,000 of capital consumed ? This would give a profit of 16·66 per cent per locomotive produced. But this is not at all the way in which the firm will, and must, reckon its profits. It will reckon its profits on its total capital, in this case £106,000 (£100,000 of fixed capital in the plant, and £6,000 of circulating or working capital in raw materials, depreciation, and labour). This gives a rate of profit of  $\frac{1,000}{106,000}$ , or just over ·9 per cent on its total capital per locomotive produced. This seems very low. But then our firm will certainly produce more than one locomotive a year. Let us say that it produces 100 locomotives a year. Then its total capital outlay is £100,000 of fixed capital and £600,000 of circulating capital (£6,000 for each of the 100 locomotives).<sup>2</sup> Its margin of price over cost for each locomotive was £1,000. So its profit was  $\frac{100,000}{700,000}$ , or 14½ per cent.

If, then, between 14 and 15 per cent was the prevailing rate of profit in industry, £1,000 would be about the amount which the firm could add to the cost price of each locomotive without attracting fresh capital, and so fresh competitors, into the industry. Thus the price of the locomotive would fluctuate according to the state of the market round the figure of £7,000.

Marx called this average, long term price, "the price of production" of the locomotive. It is made up, remember, of the

<sup>1</sup> Another thing which may make the conception of an average rate of profit difficult for the contemporary reader is the existence to-day of semi-monopolistic conditions in certain fields. In these fields, of course, the laws of competitive capitalism are modified and a rate of profit above the average can be maintained so long as the monopoly can be kept inviolate.

<sup>2</sup> Assuming that it is paid for the whole batch of 100 locomotives at the end of the year. If it is paid more frequently it will be able to do with less circulating capital.

commodity's cost of production plus an average amount of profit. Evidently this price of production is a very real thing. For, as we have seen, this amount must be forthcoming if the production of locomotives is to be maintained. If the price that they will fetch falls below this figure, the supply will at once begin to dry up. For, as we saw in Part I, an average amount of profit was, in the long run, just as necessary a part of what the capitalist economists called "the supply price" of a commodity as was a sum necessary to buy the raw materials or pay the wages.

So much for "the price of production." We can now go on to define Marx's categories of constant and variable capital. Now Marx did not deny that the categories of fixed and circulating capital were the appropriate categories to use for the capitalist's purposes. If your object is to calculate depreciation: to discover what a product has cost to make, or to calculate your rate of profit in making it, then the categories of fixed and circulating capital will serve. But, Marx declared, these categories will not serve, if your purpose is to understand "the law of motion" of the capitalist system. Those categories will not serve if you wish, for instance, to discover whence profits arise. In fact, they might have been expressly designed to conceal the source of profits. Marx, therefore, devised two new categories into which any particular investment of capital—any "capital," as he phrased it, meaning any individual lump of capital operating as the total resources of a particular firm—could be divided. These categories were constant capital and variable capital. Variable capital means the capital used to pay wages. Constant capital means all the other capital, such as the capital used to buy the raw materials and to build the plant.

These two categories cut across our former categories of fixed and circulating capital. Take our example. In the building of the locomotive, only the £1,000 paid to the workers for the necessary 10,000 man-hours of work at a wage of 2s. an hour is variable capital. All the rest, the £100,000 of plant (including the £100 of depreciation), and the £4,900 of raw materials, etc., is constant capital. So for the building of our locomotive, £105,000 of constant capital and £1,000 of variable capital were used.

We may compare these two ways of dividing up the total

capital. The capitalist categories give us—£100,000 of fixed capital plus £6,000 of circulating capital. Marx's categories give us—£105,000 of constant capital and £1,000 of variable capital. We see, therefore, that Marx's categories separate off the capital used to buy the raw materials from the capital used to pay wages, and lump together the capital used to buy raw materials with the capital used to build the fixed plant. The capitalist categories, on the other hand, separate off the capital used to buy raw materials from the capital used to build the fixed plant, and lump together the capital used to buy raw materials with the capital used to pay wages. This is the essential difference. For Marx maintained that it was by lumping together the capital used to buy raw materials and the capital used to pay wages that the source of profit was concealed. It was only by separating off from all the rest the capital used to pay wages, under the head of variable capital, that the essential nature of the system could be revealed.

For what did Marx mean by his names, constant and variable capital? He meant by constant capital, capital which remained constant in value during the process of production. And he meant by variable capital, capital which varied in value during the process of production. Constant capital was a sterile, inanimate kind of capital. Variable capital was a living, or, as he said, "organic" kind of capital; a creative capital, a capital which varied, and varied upwards, in value during the course of the process of production. He meant that all of the new value which was created in producing the locomotive out of its raw materials was created by the 10,000 man-hours of labour which the job took. Hence the capital, the £1,000, which paid for the labour of these workers, was the only capital which increased, or varied in magnitude. This capital, and this capital alone, created the additional £1,000 of value which was the profit on the locomotive. We realize that Marx's terms constant and variable do not mean anything even remotely analogous to what the terms fixed and circulating mean. The word constant sounds as if it had something to do with the word fixed, and the word variable as if it had something to do with the word circulating. Hence we are at first sight tempted to suppose that Marx was thinking of something at any rate similar

to what the capitalist categories imply : that he meant that in some way the constant capital did not circulate with the commodity and that the variable capital did. But this is not so.

These categories of constant and variable capital are a necessary corollary of the labour theory of value. If it is true that value is socially necessary labour time, then it follows that the new value created in the production of a commodity must be created by the work done on the job and by nothing else. But what about the rest of the value of a commodity ? Our locomotive, for instance, was sold for £7,000, not £2,000. Clearly the labour done on it did not create all this value. Naturally not. We did not say that the work done on the job of building the locomotive had created all its value. We said that it had created all its *new* value. We did not say that the constant capital added no value to the commodity. We said only that it added no *new* value. We see whence the remaining £5,000 of the value of the locomotive comes from. It comes from the £4,900 of necessary raw materials, fuel, machine oil, etc., which the firm had to buy and the £100 of wear and tear of the plant. But this part of the capital has merely transferred its value to the product. It was worth £5,000 at the beginning of the process of production. It is still worth £5,000 at the end of the process of production. Therefore it is constant capital. But the £1,000 spent on buying 10,000 man-hours of labour time has become at the end of the process £2,000. Therefore it is variable capital.

#### SUMMARY OF CHAPTER XIII

Marx at liberty to define value as socially necessary labour time. The issue then becomes, is the category value, when so defined, significant ? In order for it to be significant, it is necessary to explain the relationship of prices to the socially necessary labour time contained in commodities.

The best way of doing this is to see how Marx uses his category value and the other categories of economic thought which he builds upon it. Surplus value is the first of the consequential categories. Surplus value defined as value transferred from those who create it by working to those who receive it by

"waiting." How the capitalist class acquires these values very briefly described. Marx's three other consequential categories, *viz.* constant capital, variable capital, and the price of production. Constant and variable capital contrasted with the capitalist categories of fixed and circulating capital. Different ways of dividing up the capital of a locomotive building firm. Unexpected way in which the selling price of the locomotive is arrived at. The repulsion and attraction of capital between different industries. An average rate of profit, allowing for risks, must establish itself over all industries. The price of production defined. Constant and variable capital defined. Variable capital alone varies or increases during the process of production. Constant capital remains constant in value during the process of production.

## CHAPTER XIV

### *Surplus Value and Profit*

WE are now in a position to elucidate the distinction between surplus value and profit. This is a vital point, we shall find, because the proportion which the rate of surplus value must bear to the rate of profit, if Marx's argument is correct, leads straight to that famous "difficulty" which has been called "the Great Contradiction." Marx gave the name of surplus value to the £1,000 of new value which was created by the making of the locomotive. We saw, however, that this same £1,000, when looked at from the angle of the capitalist categories of fixed and circulating capital, was called profit. Apparently, then, surplus value and profit are merely the same sum compared to different things. The £1,000 represented a rate of .9 per cent of profit made by the firm on its total capital, on each locomotive produced (or  $14\frac{2}{7}$  per cent on the 100 locomotives built per year).

But it also represented a rate of surplus value of 100 per cent. For in this case we compared it with the variable capital used by the firm alone. And the firm's variable capital was itself only £1,000. Thus the same sum compared to the variable capital of a given firm is its surplus value, and compared to the total capital of the same firm is its profit. Thus we have established a ratio, or proportion, between surplus value and profit. The rate of profit must equal the rate of surplus value multiplied by the proportion of variable to total capital employed by a firm. See how it works out in this case. The rate of profit made on each locomotive is .9 per cent.<sup>1</sup> The rate of surplus value is 100 per cent. The ratio of variable to total capital is  $\frac{1,000}{106,000}$ . Therefore  $\frac{1,000 \times 100}{106,000}$  ought to equal the rate of profit. And in fact  $\frac{1,000 \times 100}{106,000} = .9$  per cent (to one place of decimals). Here we have an important relationship established. The rate of profit equals the rate of surplus value multiplied by the proportion of variable to total capital. If you are fond of algebra, as Marx was, you will write

<sup>1</sup> .9 per cent is the rate of profit on the total capital of the firm made by the production of one locomotive. In other words, this will be the actual annual rate of profit of the firm if only one locomotive is turned out per year.

it as an equation (an equation is a determinate relationship), thus  $p' = s' \frac{v}{C}$ , where  $p'$  is the rate of profit,  $s'$  the rate of surplus value,  $v$  the variable capital and  $C$  the total capital. (The dashes, as  $p'$  as opposed to simple  $p$ , mean *rate* of profit as opposed to profit.) But, if you are not fond of algebra, you will not. The point is just as easy to express in words as in symbols, only, of course, it takes a little more space.<sup>1</sup>

Where have we got to, then? The sale price of the locomotive was £7,000. This sum was made up of £6,000 of costs and £1,000 of profit. But £7,000 also expressed the value of the locomotive. This value was made up as to £5,000 of raw materials, etc., and depreciation. This part of the value simply reappears at a constant figure in the value of the locomotive. But what about the other £2,000? £1,000 of it, we know, was the value of the labour power which was used up on the job. And the other £1,000 was the new value which this labour power itself created, in the actual assembling of the locomotive out of its raw materials. It was the value of the *labour*, as opposed to the value of the *labour power*. This illustrates Marx's basic distinction between the value of the labour done on a commodity and the value of the labour power which performed this labour. The value of the labour power is, as we know, determined by the amount of necessities needed to enable the labourers and their descendants to maintain this output of labour power in perpetuity. But this labour power adds more than this amount of value to the stuff on which it works. In our example we assumed that it added twice as much.

Thus we see that the value of the commodity is determined by the amount of socially necessary labour time used up in producing it, *not* by the amount of socially necessary labour time paid for. 10,000 hours of labour power were paid for in building the locomotive at the rate of 2s. an hour. But this labour power was creating value at the rate of 4s. an hour. We know this because it raised the value of the raw materials by £2,000. And half this £2,000, viz., £1,000, since it was not paid for, is the amount of the profit or surplus value, call it whichever you like, which the firm makes per locomotive produced.

<sup>1</sup> Engels has a footnote in which he tells us that Marx was *very* fond of algebra. However, he was bad at arithmetic and Engels had to check all his sums for him.

Thus everything seems to balance and tally nicely. The sale price of the commodity and its value are the same, namely, £7,000. And so is the amount of profit and the surplus value, namely, £1,000. Naturally the rate of profit and the rate of surplus value are very different. But that is only because they are arrived at by comparing the same sum, £1,000, to two very different quantities, to the variable capital and to the total capital respectively. The variable capital is itself only £1,000, so our £1,000 of surplus gives a rate of surplus value of 100 per cent ; the total capital is £106,000, so the same £1,000 surplus gives a rate of profit of .9 per cent. Surplus value and profit are apparently merely different ways of looking at the same thing. The labour theory of value and the categories consequential upon it seem to explain the observed situation, namely, the formation of prices, the origin of profit and kindred questions, very adequately.<sup>1</sup>

Marx points out that capitalist production is carried on exclusively for the sake of the production of this thing, called surplus value if you compare it to the capital which the capitalist had to use in order to pay wages, or called profit if you compare it to all the capital which he had to use. "The product in which the capitalist is really interested is not the tangible product itself, but the excess of the value of the product over the value of the capital assimilated by it," he writes. (Vol. III, p. 54.)

But if the capitalist cares everything, Marx continues, for the existence of this thing, this "excess," he cares nothing for its name. He cares not at all for any nice distinction of the sort we have been drawing between profit and surplus value. Still, he does know which is the relevant comparison for him, with the capital he has paid out in wages or with all the capital which he has used. He knows that what matters to him is how much money he has made *in proportion to his total capital*. It is no use to him to have made £10,000 instead of £9,000 if he has had to use, say, £1,000,000 of capital instead of £100,000 in order to get the extra £1,000 profit. He would have done better to have invested the extra £900,000 of capital elsewhere. It is the *rate of profit* on his total capital which interests him. Nor

<sup>1</sup> We devote the next chapter to a consideration of the great contradiction said to be involved in this analysis.



does the alleged fact that the profit all comes from one particular part of his capital, from the capital which he uses to pay wages, seem to him to have any practical significance. For it has been admitted that in order to use this wage paying (variable) capital he has to lay out the rest of his capital.<sup>1</sup>

We begin to see that a capitalist, if he ever read Vol. III of *Capital*, would say that Marx's categories and distinctions might or might not be true, but that in any case they had not the slightest importance. The capitalist is desperately interested in the creation of a surplus. But, as Marx writes, "the definite relation of this surplus, and its internal connection, with the various components of capital" does not interest him. Moreover, we have so far only revealed one half of the considerations which make, and which always have made, the Marxian category of surplus value of indifference to the individual capitalist.

We have seen that the amount of surplus value which a capitalist can make only matters to him in proportion to the amount of capital (of all sorts) which he has to use in making it. But it is not even true to say that what matters to a capitalist is the amount of surplus value he makes in proportion to the amount of capital he uses. For the extraction of surplus value from the process of production is only half of the capitalist's battle. It is now time to call the reader's attention to the fact that we have all along been assuming that the commodities made by the capitalist actually do fetch their value when they are taken to market. The locomotive in our little example had a value of £7,000 and we assumed that it actually fetched £7,000. But as we have already seen, this would only be true "in a state of equilibrium," when capital was neither being attracted into or

<sup>1</sup> "It is immaterial," as Marx puts it, "for the capitalist whether he is supposed to advance constant capital in order to make a profit out of his variable capital, or whether he advances variable capital in order to make a profit out of the constant capital; whether he invests money in wages in order to make his machinery and raw materials more valuable, or whether he invests money in machinery and raw materials in order to be able to exploit labour. Although it is only the variable portion of capital which creates surplus-value, it does so only on condition that the other portions, the material requirements of production, are likewise advanced. Seeing that the capitalist can exploit labour only by advancing constant capital, and that he can utilize his constant capital only by advancing variable capital, he lumps them all together in his imagination, and he is all the more apt to do so as the actual rate of his gain is not calculated on its proportion to the variable, but on its proportion to the total capital, in other words, that it is calculated on the rate of profit, not on the rate of surplus-value." (*Capital*, Vol. III, chap. ii, pp. 54-5.)

repulsed from the locomotive-building industry.<sup>1</sup> But there is no guarantee that in practice this state of things will exist. On the contrary, a new invention (*e.g.*, the growing use of the motor omnibus) may have drastically decreased the community's need for locomotives. Down goes their price. *Down goes their price to below their value.* The locomotive-building capitalists may duly have extracted £1,000 of surplus value from the process of production; but they may be quite unable to realize any of this surplus value when they take their locomotive to market. Hence, although each capitalist is interested in producing the maximum amount of surplus, the maximum lump of new value in proportion to his total investment of capital, this is not the only thing which interests him. In present day conditions it is often not even his principal interest.

For it is no good to the individual capitalist to have produced a large amount of new value with a small investment of capital—unless he can turn that lump of value into hard cash: unless he can sell it. The lump of new value is embodied, remember, in a supply of commodities. But no one has guaranteed that the capitalist will actually be able to sell these commodities at their value. There may be a glut of them. Their price may drop to half their value. The capitalist may not be able to retain for himself any of the new value which has been embodied in them. This may not mean that this new value will be destroyed. It may merely mean that someone else, maybe some other capitalist, will get hold of it. For example, say that circumstances arise in which there is a glut of steel. Let us suppose that the glut is so bad that the steel producers cannot realize, cannot get the price of, any of the new value which they have created in making the steel. They have to sell to the engineering firms which buy their steel, at bare cost. Does that necessarily mean that the new value of the steel is lost? Not at all. It is acquired by the lucky engineering firms. They get their raw materials unexpectedly cheap. And they, if they are quick, may be able to realize the new value which the steel producers failed to retain, as well as the value which they themselves have added, when they sell their finished commodities. In capitalist language, the profits which should

<sup>1</sup> As we shall see in the next chapter, it is not true for particular commodities even then.

have gone to the steel firms have gone to the engineering firms. In periods of disturbance such cases of one capitalist, or capitalist group, purloining the values produced by another, frequently occur, and they may in part persist until the transfer of capital from one industry to another can put the matter right.

So we see that value and surplus value are indeed queer, far away categories from the point of the individual capitalist. In the first place, the amount of surplus value made by a capitalist only matters to him in proportion to the total amount of capital which he has had to use in making it. In the second place, the amount of surplus value which each capitalist produces is often not so important a question for him as the amount of surplus value which he can, by luck or skill, extract from a competitor by selling above value and buying below value.

Still, the amount of surplus value created in the process of production is by no means a matter of indifference to the capitalists as a class. The amount of surplus value, remember, depends on the difference between the values which must be given to the workers by way of wages and the values which the workers create. Hence for the capitalists as a class, if not for the individual capitalist, this amount is of the very first importance. For this is the sole source, the unique pool, out of which all the capitalists and their friends can draw their profits, etc. For each particular capitalist his own share in the pool may be far more important than the total size of the pool. But for the capitalists as a body the size of the pool is what matters. And this distinction is strikingly exemplified by practice. For the increase of the total size of the pool is the one purpose for which competing capitalists will, and do, unhesitatingly unite. The size of the pool of surplus value out of which the capitalists and their friends may each draw what his wits and his luck enable him, is primarily dependent upon the rate of wages. At any given moment (at any given price level) the size of this pool will depend on how low wages can be kept.

And, precisely for this purpose of keeping down wages, even the most furiously competing capitalists will always unite. Nothing could be more striking in this connection than the conduct of the British mine-owners during the last ten years. The British mining industry is conducted by over a thousand

furiously competing companies and firms. These firms for years resisted by every conceivable means the various attempts on the part of the British Government to unite them. But there is a purpose for which they have long ago achieved unity by themselves (in the coal owners' associations) without the least need for any pressure from anyone—bargaining over wages with the British miners.

Here, then, is the exact practical expression of the underlying economic reality. The British mining capitalists know that the size of the pool of surplus value out of which they can draw their profits depends, other things being equal, upon how low they can keep the miners' wages. Hence for this object they pull together in perfect unison. But they know equally well that the particular share which each can extract from this pool depends on the contrary, upon their skill and luck in defeating each other, and the other capitalist groups, in competitive struggle.

The rate of profit which a particular capitalist makes is thus doubly removed from the surplus value which he himself extracts. First his rate of profit will depend on how much capital he had to lay out to get this amount of surplus value. Second his profit will depend on how much of this surplus value he can retain in the general competitive scramble. Is it any wonder, then, that the capitalists protest that Marx's categories have little or no significance? These protests are, however, strikingly belied, on those occasions on which the capitalists act, not in their individual interests, but all together and in unison.<sup>1</sup>

<sup>1</sup> It may be well to give Marx's own recapitulation of the relationship between profit and surplus value, and the way in which the category profit obscures the origin of the capitalists' incomes. The passage is one of his fullest, but not one of his easiest.

"While the rate of profit differs numerically from the rate of surplus-value, the profit and the surplus-value are actually the same thing and numerically equal. However, the profit is a transformed kind of surplus-value, a form in which its origin and the secret of its nature are obscured and extinguished. Profit is, therefore, that disguise of surplus-value which must be removed before the real nature of surplus-value can be discovered. In the surplus-value, the relation between capital and labour is laid bare. But in the relation of capital and profit, that is to say, the relation between capital and that form of surplus-value which appears on one hand as an excess over the cost-price of commodities realized in the process of circulation, and on the other hand as a surplus determined by its relation to the total capital, *the capital appears as a relation to itself*, a relation in which it, as the original amount of value, is distinguished from a new value generated by itself. It is dimly recognized, that

## SUMMARY OF CHAPTER XIV

The distinction between surplus value and profit elucidated. The relationship of the rate of surplus value and the rate of profit defined. The rate of surplus value equals the rate of profit multiplied by the proportion of the variable to the constant capital. Surplus value and profit appear to be the same sum compared to the variable and the constant capital respectively.

Capitalist production carried on solely with a view to the production of this surplus, this excess of selling price over cost of production, call it surplus value or profit as you will. But a capitalist is uninterested in the absolute amount of the surplus value which he makes. He is only interested in this amount in proportion to the total capital which he must lay out in order to make it; he is interested, that is to say, in his rate of profit alone. Moreover the capitalists are uninterested in whence this surplus comes; in whether it comes from their variable capital alone or from all their capital.

Again a capitalist is not only interested in obtaining his surplus or profit; he is also desperately interested in retaining it for himself. Possibility that it may be filched from him by another capitalist being in a position to compel him to sell his products below their value. Value and surplus value are, thus, categories doubly removed from the interests of the capitalist.

The creation of the maximum amount of surplus value is of the highest importance to the capitalists as a class, however. This fact revealed by the existence of combinations of otherwise furiously competing capitalists for purpose of bargaining over wages. The coal owners' associations instanced. The amount of surplus value seen to be the unique pool out of which the capitalists can draw their profits. Hence the interest of all of them is to maximize this pool. The size of the profits of each individual capitalist seen, however, to depend not on how much surplus value he puts into this pool, but on how much value his luck and skill enable him to draw out of it.

capital generates this new value by its movement in the processes of production and circulation. But the way in which this is done is surrounded by mystery, and thus surplus-value seems to be due to hidden qualities inherent in capital itself." (*Capital*, Vol. III, chap. ii, p. 62.)

## CHAPTER XV

### "The Great Contradiction"

THE preceding chapter has shown us that Marx's categories of value, surplus value, the price of production, constant capital, and variable capital are of little use to the capitalists. It is enough to repeat that the rate of profit is doubly removed from the amount of surplus value, in order to establish this point. For the capitalists the only practical conclusion from the whole elaborate analysis of Marx turned out to be that it was to the interest of the capitalist class to keep down the rate of wages. And really, the capitalists may protest, we did not need this long and abstruse discourse to tell us that!<sup>1</sup>

Capitalist economists have, however, another and more precise objection to Marx's categories, and to the rational construction which he rears upon them. They say, flatly, that they are self-contradictory. The point is a simple one. Marx asserted that the lump of profit or surplus value made by a firm was exclusively produced by the variable capital employed by that firm. Thus, given the same rate of surplus value, the same degree of fertility, that is to say, in their variable capitals, the amounts of profit made by firms with equal total capitals must depend on how much variable, as compared to constant, capital they can manage to use. The more of this creative, growing kind of capital, as compared to the constant, or sterile, kind of capital, they can use, the bigger will be the amount of profit which they will make. To put the point more precisely, the rate of profit of a firm must depend, other things being equal, on the proportion of its variable to its constant capital.<sup>2</sup>

Therefore firms which can use a relatively large amount of variable capital must make higher profits than firms which

<sup>1</sup> This is an illustration of the fact that the instinctive horse-sense of the practical working capitalists and Marx's scientific analysis often reach substantially the same conclusions. These conclusions are usually opposite to those of the half-baked capitalist economic thinkers, who tell us, for example, that it is in the interests of the capitalists to pay high wages.

<sup>2</sup> The algebraically-minded would put it succinctly thus: We know that  $p' = s' \frac{v}{c}$ . Therefore  $p' = \frac{v}{c}$  if  $s'$  is assumed to be constant. ( $p'$ , we recollect, stands for the rate of profit,  $\frac{v}{c}$  for the proportion of variable to constant capital, and  $s'$  for the rate of surplus value.)

have to use a relatively large amount of constant capital. In other words, firms which employ much labour and little plant and machinery must make a high rate of profit and firms which employ little labour and much plant and machinery must make a low rate of profit. Now some branches of production are of a kind in which you must, technically, use much plant and machinery and little labour (*e.g.*, chemicals ; artificial silk) ; and other branches of production are of such a kind that you must use much labour and little plant and machinery (*e.g.*, coal mining ; agriculture). Hence the rate of profit must be much higher in coal mining and agriculture than it is in artificial silk and chemicals. But this is not the case. Indeed, we have just established the fact that in the long run the rate of profit must even itself out throughout the economic system. For if one line of business does especially well, more capital will flow into it until its profits are evened down, and if another line of business does especially badly, capital will flow out of it until its profits are evened up. So, apparently, we have proved : (i) that the rate of profit varies with the proportion of variable to constant capital used in different industries ; (ii) that some industries use far higher proportions of variable to constant capital than others ; (iii) that profits are in the long run equal as between all industries. What is to be done about this apparently glaring contradiction ? Had Marx never noticed it ? He had noticed it all right. We had better give his own statement of the point at issue.

Marx first makes it quite clear that he really does mean that variable capital, the capital that is used to pay wages, must, if the labour theory of value is true, be the only capital which produces value. (The letters *c* and *v* in this passage are Marx's shorthand for constant and variable capital. The expression “ the same degree of exploitation ” is Marx's expression for the same rate of surplus value.)

“ If a capital, consisting of percentages of 90 *c*+10 *v*, produced as much surplus value, or profit, with the same degree of exploitation, as a capital consisting of percentages of 10 *c*+90 *v*, then it would be as plain as daylight that the surplus value, and value in general, must have an entirely different source than labour, and that political economy

would then be without a rational basis." (*Capital*, Vol. III, chap. viii, pp. 176-7.)

Thus Marx nails his colours to the mast. But if the variable capital alone produces value, the rate of profit must be higher in those industries which use much variable capital. But we know that in fact it is not. The rate of profit is in the long run the same throughout the productive system. Moreover, as Marx immediately points out, it is impossible to imagine the capitalist system without this average rate of profit throughout the whole of industry.

"There is no doubt that, aside from unessential, accidental, and mutually compensating distinctions, a difference in the average rate of profit of the various lines of industry does not exist in reality, and could not exist without abolishing the entire system of capitalist production. It would seem, then, as though the theory of value were irreconcilable at this point with the actual process, irreconcilable with the real phenomena of production, so that we should have to give up the attempt to understand these phenomena."<sup>1</sup> (*Capital*, Vol. III, chap. viii, pp. 181-2.)

None of Marx's critics ever succeeded in putting the difficulty more forcibly than this. But what is the solution?

Marx solves the problem by demonstrating that the profit made by a particular firm is not all retained by that firm. The original lump of profit or surplus value, consisting of the difference between what is paid to the workers and what they add to the value of the product in the course of their work upon it, cannot be retained by the particular firm which makes it. On the contrary, the force of competition compels capitalist firms to pool this amount of profit or surplus value with all of their competitors throughout the productive system. And then from this pool each particular firm is able to draw out the amount of

<sup>1</sup> Marx, the reader will notice, considered that unless the labour theory of value could be shown to be compatible with "the real phenomena of production," we should have to give up trying to understand "these phenomena" (i.e., economics) at all. The attempt to develop an economic science without the basis of any objective theory of value is precisely what the capitalist economists have busied themselves with for the last hundred years. We exhibited in preceding chapters the plight into which they have at length got themselves as the result of these labours.



profit which will give it an average percentage of profit on its total capital. And this pooling process will take place not only when there is a sudden glut, as we saw in the last chapter, but habitually as between industries using different proportions of variable and constant capital. All this sounds remote from reality. And yet, as we saw in the last chapter, this is precisely what really does happen. Commodities are, and must be, priced at a figure which will in the long run give the firms which make them an average rate of profit on their capital. For, if they are priced above this figure, new capital, and so new competitors, will flow into the industry, and if they are priced below this figure their supply will begin to dry up because capital (or, to put it in the terminology we were using in Part I, our old friends the factors of production) will begin to seep out of the industry.

So, in spite of appearances, there is no doubt about it that Marx was right when he said that commodities have in the long run average to be sold at prices which will yield an average rate of profit on the capital which has produced them. This figure Marx called, we remember, “ the price of production.”

The price of production is, then, no airy abstraction, no queer creature of Marx’s brain, begotten of difficulties in reconciling the law of value to the facts of life, but an actual fact of everyday experience.<sup>1</sup> There is no doubt that Marx’s account of how prices are arrived at in the capitalist world is correct. The prices of commodities do fluctuate round about their price of production. “ In equilibrium ” the price of all commodities would be their prices of production.

Now we begin to see the nature of Marx’s solution of the problem. Firms which use much variable and little constant capital do *make* much more surplus value or profit than firms which use capital of an opposite composition. The commodities which the former firms produce are much the more valuable, since they contain much more human labour. But these firms cannot sell their laboriously made products at their full value. For if they did they would make a much higher percentage of profit on their capital than would the more mechanized firms.

<sup>1</sup> Mr. Raymond Postgate, in his superficial little book, *Karl Marx*, for example, pooh-poohs the idea that the “ price of production ” is anything but a strange figment of Marx’s brain.

Hence these firms have to sell their products at below their value, at their price of production in fact. Similarly the more mechanized firms are enabled to sell their products at above their value. For their products contain little human labour, and if they had to sell them at their value they would be unable to make the average rate of profit on their capital. So in their case the actual figure, the price of production, at which they sell their products is above those products' value.<sup>1</sup>

There is no doubt that Marx's solution of the problem is watertight. Variable capital (as the financial expression of human labour) is the only thing which creates value. Therefore a total capital with much variable and little constant capital in it does create much more value than a capital of opposite composition. But a capital containing much of the variable element cannot retain all the value which it has created. The force of competition drives it to share out its newly created value evenly with all the other capitals in existence. For if it did not do so new capital would pour into those industries which work with a high amount of variable capital and out of those industries which work with a low amount of variable capital.

The solution is complete. But is it not a solution which seriously exposes the labour theory of value to the old charge of insignificance? For, as the reader has undoubtedly noticed, Marx has only reconciled the labour theory of value to "the real phenomena of production" by agreeing that to-day commodities do not sell at their values. Moreover, he has shown that they do not sell at their values, even in equilibrium, even on the average, even when the fluctuations caused by supply and demand are cancelled out. Commodities, that is to say, do not even tend to exchange in proportion to the amount of socially necessary labour time embodied in them. The points round which demand and supply cause prices to fluctuate are not the values of commodities, but their prices of production. What, then, has become of the concept, value? What connection with reality can it still maintain?

<sup>1</sup> "A capitalist selling his commodities at their price of production recovers money in proportion to the value of the capital consumed in their production and secures profits in proportion to the aliquot part which his capital represents in the total social capital. His cost-prices are specific. But the profit added to his cost-prices is independent of his particular sphere of production, for it is a simple average per 100 of invested capital." (*Capital*, Vol. III, chap. ix, p. 187.)

The reader will notice that we are back at the old question with which the post-classical economists believed that they had defeated Ricardo. Why, they asked, if labour determines value, do not even the average prices of commodities correspond to the amount of labour which has been embodied in them? Marx has certainly given a clear and full answer to that question. The prices of commodities do not fluctuate round their values, around, that is to say, the quantity of socially necessary labour time embodied in them, because in modern conditions they are produced by capitals of varying “ organic composition.” Some commodities, that is to say, are produced in highly mechanized conditions employing expensive plant and machinery, while others are produced in relatively unmechanized conditions with much labour but little plant and machinery. Accordingly, since the competition of capitals is bound to level out the rate of profit, prices are forced away from values and caused to fluctuate round “ prices of production ” instead. For whatever reason, however, the admission has now been made that value, determined by socially necessary labour time, is not the point round which prices fluctuate. Is not Marx, then, in almost as great a difficulty as was Ricardo? He has, it is true, saved his concept value, but has he not done so only by rupturing all connection between it and reality? Has not the category value, defined as socially necessary labour time, been shown to be an empty abstraction, without real application or significance? This is the argument of all those of Marx’s capitalist critics who have taken the trouble to read the third volume of *Capital*. It is, in particular, as we shall see, the line of argument adopted by much the ablest of them, Professor Böhm-Bawerk, in his well-known essay, *Karl Marx and the Close of His System*.

What is Marx’s answer to this allegation? Once again it is essential to remember what it is that Marx is trying to do. He is trying to discover “ the law of motion ” of the capitalist system. He is trying to show what will be the consequences of the continued working of that system upon the basis laid down for it, both in practice and in theory, by the capitalist class. He is *not* trying to discover the consequences of particular modifications of that basis, of the imposition of a tariff here or the

devaluation of a currency there, or the institution of unemployment insurance in another place.<sup>1</sup> The task to which Marx devoted his life, and to which all three volumes of *Capital* are strictly confined,<sup>2</sup> is the establishment of what are the inherent tendencies of the capitalist system as such. The very title of Volume III is significant in this respect. It is "Capitalist Production as a Whole." Thus the subject matter of the volume is clearly announced to be the essential nature, and therefore destiny, of the system itself. In particular, it is to "Capitalist Production as a Whole," and to this alone, which Marx applies the labour theory of value.

We have just seen that the points around which the prices of particular commodities fluctuate (namely, their "prices of production") differ from their values. We have further shown that their prices of production differ from their values to the extent to which the ratio of variable to constant capital differs from the average in the capital of the particular firm which produced them. If the ratio of variable to constant capital is high, then the price of production is below the value, if the above ratio is low, then the price of production is above the value. Hence it follows that commodities which *are* produced by firms, whose capitals happen to contain just the average ratio of variable to constant capital, are sold, "in equilibrium," at their values.

Marx now asks us to think of, say, five different capitals<sup>3</sup> each of a different composition (each containing a different proportion of variable to constant capital). If none of these capitals happens to have a composition just equal to the average composition of all five taken together, the commodities produced by these five capitals will all sell at prices either above or below their values, according to whether there is much or little of the variable component in the particular capital which produced

<sup>1</sup> This is not to say that the discovery of the law of motion of the system itself, of the system as a system, unmodified and unadulterated, of the system "in equilibrium" (as the capitalist economists would put it), will not throw light on the consequences of particular modifications. Indeed we shall not be wrong in supposing that until and unless the essential law of the unmodified system has been established we shall never be able to understand or predict the consequences of particular modifications.

<sup>2</sup> With the partial exception of chapter x of Vol. III, as we shall see.

<sup>3</sup> The capitals of five different firms, that is to say.

them. Each of their prices will differ from each of their values. But will all their prices differ from all their values ? They will not, Marx writes. For if you add all these capitals together, you will be able to find out what is the ratio of variable to constant capital in them taken all together. Therefore the total prices at which all the commodities produced by this total capital will sell, will add up to their total values. But why confine this conclusion to these particular five capitals ? If it is true for them that they must have an average ratio of variable to constant capital, is it not true for all the capitals in existence in the entire economy ? Of course it is. There must be at any particular time an average ratio of constant to variable capital employed in the entire productive system.

Indeed we know that this ratio exists because we are aware of its gradual change. As everybody knows, the history of capitalism has been the history of the gradual transformation of production from a simple, laborious, handicraft basis to a labour saving, complicated, mechanized basis. But this is only another way of saying that the average ratio of variable to constant capital used in the whole economy has been getting smaller and smaller.

Well, then, if there is for the entire social capital at any one time a particular ratio of constant to variable capital, then it follows that the sum of the prices of all the commodities produced must equal the sum of their values. (Or, more exactly, of course, that the sum of their prices “ in equilibrium,” the sum of their “ prices of production,” must equal their values.) Marx writes it thus : “ The sum of all the prices of production of all commodities in society, comprising the totality of all lines of production, is equal to the sum of their values.” (Vol. III, p. 188.) At length, then, we see how it is that the labour theory of value applies to the “ real phenomena of production.” It applies to these phenomena as a whole, as a system.

In particular, it applies to the difference between the total value or price of all the commodities produced, and the total value or price of all the labour power used, in a given economy. Or rather, it applies to the relationship which this difference, or margin, has to the total capital employed by the economy in question. Marx was interested in this relationship above any

other because he looked upon changes in it as the determinant of the rate of profit. For the difference between the total value of all the commodities produced by a capitalist society and the total value of all the labour power used in that society, is surplus value. And, as we have seen, the amount of surplus value produced in a capitalist society constitutes the unique pool out of which the capitalist class can draw its profits. Hence the average rate of profit maintained by a capitalist economy depends upon the total amount of surplus value realized, compared to the total amount of capital used. The average rate of profit =  $\frac{\text{Total surplus value}}{\text{Total capital}}$ . Thus the rate of profit can be affected by a change in the magnitude of either the total surplus value realized or the total capital used. For instance, the rate of profit would drop even though the total surplus value increased, if at the same time the total capital used increased still more. Hence any shrinkage in the margin between the total value of the commodities produced and the labour power used, in proportion to the total capital employed, constitutes a menace to the maintenance of the rate of profit, and so to the very existence of a capitalist economy.

Thus a law which makes it possible to determine these three quantities, viz., the total value of all the commodities produced, the total value of the labour power used, and the total value of all the capital employed, in a given society, alone makes it possible to understand what is happening to that economy. This is the solution of "the Great Contradiction."

Let us state the point again.<sup>1</sup> Marx says that, though particular commodities do not sell at their values, do not exchange even in equilibrium, that is to say, in proportion to the amount of socially necessary labour time contained in them, yet the sum total of all the commodities produced is made up of the units of socially necessary labour time contained in them. Consequently what prices represent, though for each particular commodity

<sup>1</sup> How necessary it is to emphasize this point may be gathered from the fact that Professor Sidney Hook has overlooked it. He tells us (*Towards an Understanding of Karl Marx*, p. 171) that the essential point is that commodities sell at their values when they are produced by capitals of average composition. But he fails to point out that the sum of commodities is inevitably produced by a capital of "average" composition. And this is the only point that matters.

imperfectly, are these units of socially necessary labour time. The labour theory of value bids us ascertain the amount of socially necessary labour time contained in commodities if we would know their value. And it is by knowing the value of commodities alone that we shall be able to add commodities up into totals which have a meaning. And unless we can add up commodities into significant totals we shall never be able to understand what is happening to the capitalist system. But the labour theory of value will not tell us the ratios at which particular commodities will exchange in modern conditions. This is clear once we have realized that it is only to the sum total of commodities that the labour theory of value applies. For something which is true of a total alone can have, by definition, no application to the relationship of the parts of that total *inter se*.

We have said that the total value of commodities equals their total prices. *But, unless we realize that prices represent real quantities, viz., amounts of socially necessary labour time, a total of prices is a meaningless expression.* We recollect Professor Robbins' view that “ the valuations which the price system expresses are not quantities at all.” And we recollect the pitiable plight into which this view led him. The valuations which the price system expresses (however imperfectly) are quantities of socially necessary labour time. Moreover, the fact that as production becomes more and more technically developed the price system expresses these valuations more and more imperfectly is, as we shall see, just what is at the bottom of the irremediable troubles of the capitalist system. It is this ever growing divergence between prices and values which is causing the system to produce ever more irrational, anti-social, and finally murderous, results. We saw in Part II that the monstrous results which the present system produces flow from the fact that existing money costs bear little relation to the true efforts and sacrifices undergone, the actual work done, in the production of commodities, and that existing money offers bear little relation to human needs. And these divergences are a reflection of the fact that the prices of commodities are increasingly diverging from their values, are increasingly diverging, that is to say, from the quantities of socially necessary labour time contained in commodities. For if commodities could be priced so that they sold at their value,

costs would be brought back into direct relation to human effort. And in the same way demand would once again express human needs, for the money spent in production would be distributed to the men and women who did the work, instead of, in a great part, to the persons who "waited" for the dividends.

The point that prices are ratios and that consequently a total of prices is a meaningless expression is seized upon by Böhm-Bawerk in his famous onslaught on the third volume of *Capital* ("Karl Marx and the Close of His System"). He has a passage which must seem devastating to those who have not read Marx or, having read him, have not understood that the whole purpose, the "*quæsitum*," to use the economists' term of art, of *Capital* is fundamentally different from the *quæsitum* of the works of post-classical capitalist economists.

Böhm-Bawerk's object is to show the insignificance of the expression "total prices." For him prices are the exchange relationship between commodities, and nothing else. Prices are simply the numerical expression of those ratios of exchange. And, of course, you cannot have a total of ratios! The object of any law of value must be, Böhm-Bawerk writes, to explain the exchange relationship of commodities. Let us quote him *in extenso*, for his is the best statement of the capitalist attack upon Marx and may well stand for all those who have subsequently, and usually not even accurately, copied out his arguments.

"There can clearly only be a question of an exchange relation between different separate commodities among each other. As soon, however, as one looks at all commodities as a whole and sums up the prices, one must studiously and of necessity avoid looking at the relations existing inside of this whole. The internal relative differences of price do compensate each other in the sum total. For instance, what the tea is worth more than the iron the iron is worth less than the tea and *vice versa*. In any case, when we ask for information regarding the exchange of commodities in political economy it is no answer to our question to be told the total price which they fetch when taken all together, any more than if, on asking by how many fewer minutes the winner in a prize race had covered the course than his competitor, we were to be told that



all the competitors together had taken twenty-five minutes and thirteen seconds.

“The state of the case is this : To the question of the problem of value the followers of Marx reply first with their law of value, *i.e.*, that commodities exchange in proportion to the working time incorporated in them. Then they—covertly or openly—revoke this answer in its relation to the domain of the exchange of separate commodities, the one domain in which the problem has any meaning, and maintain it in full force only for the whole aggregate national produce, for a domain therefore in which the problem, being without object, could not have been put at all. As an answer to the strict question of the problem of value the law of value is avowedly contradicted by the facts, and in the only application in which it is not contradicted by them it is no longer an answer to the question which demanded a solution, but could at best only be an answer to some other question.

“It is, however, not even an answer to another question ; it is no answer at all ; it is simple tautology. For, as every economist knows, commodities do eventually exchange with commodities—when one penetrates the disguise due to the exchange of money. Every commodity which comes into exchange is at one and the same time a commodity and the price of what is given in exchange for it. The aggregate of commodities therefore is identical with the aggregate of the prices paid for them ; or, the price of the whole national produce is nothing else than the national produce itself. Under these circumstances, therefore, it is quite true that the total price paid for the entire national produce coincides exactly with the total amount of value of labour incorporated in it. But this tautological declaration denotes no increase of true knowledge, neither does it serve as a special test of the correctness of the alleged law that commodities exchange in proportion to the labour embodied in them.”

The first thing that Böhm-Bawerk proves in this passage is that Marx's law of value will not tell you the ratios at which commodities will exchange. It will not answer questions of the following kind—“If so and so happens, will the price of wheat

rise and the price of iron fall ? ” And the next thing which Böhm-Bawerk proves is that he cannot conceive of there being any other kind of questions in economics. For Böhm-Bawerk, as for every capitalist economist since his day, economics is the elucidation of the exchange relationship of commodities ( “ given,” as Professor Robbins puts it, “ the facts of the legal and technical environment ” ). Now for this purpose it is perfectly true that a series of equations expressing demand and supply is what is needed. And it is perfectly true that for this purpose the category value, as determined by socially necessary labour time, is insignificant. *But then this was not the purpose for which Marx devised and used it.* At the risk of wearisome repetition, let us say once more that Marx devised his whole theoretical construction in order to ascertain the law of motion of the capitalist system. And this law cannot be deduced from a study of the exchange relationship of commodities.

Indeed, it is not too much to say that an economic science built up from a study of the exchange relationship of commodities is bound to obscure finally the true nature, and the law of motion, of capitalism as a system. In chapter x of Vol. III Marx turns aside from his main theme and briefly exhibits the way in which prices are formed on the market. It is against this chapter that Böhm-Bawerk directs much of his attack. He complains bitterly that it is scrappy and inconclusive, “ uncertain,” and “ dilatory.” Then he adds this interesting comment on it.

“ If at the time when he ” (Marx) “ was dealing with actual exchange relations—those manifested in real life—he had pursued the subject with the same luminous penetration and thoroughness with which he followed, through two volumes, the hypothesis that value is labour to its utmost logical conclusion ; if at this juncture he had given to the important term ‘ competition ’ a scientific import, by a careful economic-psychological analysis of the social motive forces which come into action under that comprehensive name ; if he had not halted or rested, so long as a link in the argument remained unexplained, or a consequence not carried to its logical conclusion ; or so long as one relation appeared dark and

contradictory—and almost every word of this tenth chapter challenges a deeper enquiry or explanation such as this—he would have been driven step by step to the exposition of a system altogether different in purport from that of his original system, nor would he have been able to avoid the open contradiction and retraction of the main proposition of the original system.”

What Böhm-Bawerk wanted was that Marx should have written a full-dress treatise of marginal utility economics. For that is what an approach to the subject based upon “ a careful economico-psychological analysis ” of competition leads to. And no doubt Böhm-Bawerk was perfectly right in believing that Marx could have written a brilliant work of this kind.<sup>1</sup> Marx could have elaborated his equilibrium equations with the best of them. There is no doubt of it, and there is also no doubt that, if he had done so, he would have arrived at “ a system altogether different in purport from his original system.” For a theoretical structure which bases itself upon the phenomena of competition, upon the fluctuations of demand and supply, is incommensurable with a structure such as Marx’s, which bases itself upon a theory of value, a theory of some underlying common factor in commodities which renders them commensurable. Böhm-Bawerk was aware of this. “ Modern political economists agree,” he wrote, “ that the old scholastico-theological theory of ‘ equivalence ’ in commodities to be exchanged is untenable.” They do : and we have seen the sterility and impotence into which this abandonment of an objective theory of value has landed them.

There are, then, two incommensurable structures of economic thought. Both claim that “ the real phenomena ” of life can be subsumed under their respective generalizations. (Or, rather,

<sup>1</sup> Böhm-Bawerk calls Marx “ an intellectual force of the very highest order,” and then accuses him of errors which would disgrace a numbskull. The same difficulty recurs in the case of nearly all Marx’s capitalist critics. Mr. Carr, his latest English biographer, for instance, tells us that Marx was not a great philosopher, was nothing of an economist, and was certainly not a statesman, nor an orator, nor a leader of men (*Karl Marx*, p. 300). On the next page, however, he tells us that Marx was perhaps the first man since Luther “ whose life has constituted a turning point in human thought.” It is all very peculiar. Everything Marx said was nonsense, everything he did was futile, and yet somehow or other his words and deeds overshadow in importance the words and deeds of any figure of the last five centuries.

both used in Böhm-Bawerk's time to make this claim. For, as we saw in Chapter I, capitalist economists no longer even claim that the overwhelmingly important phenomenon of crisis can be accounted for by their science.) Capitalist economics concentrates its attention upon price, upon the exchange relationship of commodities. Marxist economics concentrates its attention upon value. The one is predominantly a theory of exchange; the other is predominantly a theory of production.<sup>1</sup>

But which of these two incommensurable structures of economic thought is relevant to reality? Which approach, that based upon "an economico-psychological" analysis of competition, or that based on an objective theory of value, gives us true insight into the nature of our economic system? Which enables us to predict what will happen to that system? Has the science built up by Böhm-Bawerk and his colleagues upon an economico-psychological analysis of competition, or has the science built up by Marx and his successors upon the basis of the labour theory of value, best enabled their respective adherents to comprehend the present and to predict the future? This is the decisive test.<sup>2</sup>

<sup>1</sup> I take this contrast from the unpublished paper by Mr. J. D. Bernal, which is cited at the beginning of this Part.

<sup>2</sup> Professor Sidney Hook dissenting as follows:

"The significant point to be made here, however, is that no matter what the deliverances of market experience are, the labour theory of value can be saved. But why save it? Some have claimed that it should be saved for the same reason that any other scientific hypothesis should be saved, that is to say, because of its power to predict. Yet neither the labour theory of value nor any other theory of value can predict anything which is not already known in advance. War and crisis, centralization and unemployment, were already quite familiar phenomena when Marx reformulated the theory of value. He could show that their existence and increasing frequency were compatible with that theory and that the most significant phenomena of economic life could be described in its terms. It is a mistake to believe, however, as, for example, Bukharin does, that one can predict anything *specific* on the basis of the labour theory. That wars and panics will occur and capitalism break down are propositions too general to be enlightening: for unless these events are given *specific temporal co-efficients*, it can be shown that they follow just as readily from economic assumptions other than those used by Marx." (*Towards the Understanding of Karl Marx*, by Sidney Hook, chap. xv, p. 187.)

This passage is fallacious from beginning to end. The labour theory of value is valueless unless it does give us power to predict. It is not valueless because it does not, in itself, give us the power to date exactly the fulfilment of our predictions. "That wars and panics will occur and capitalism break down" are not "propositions too general to be enlightening." On the contrary, our whole conduct as rational beings must hang on whether we accept these propositions or not. For it is flatly untrue that these propositions "follow from economic assumptions

We investigated in Parts I and II of this book the degree to which the capitalist science of economics, built up upon the study of the exchange relationship of commodities, enabled its adherents to comprehend the present or predict the future. We found that it was not until its practitioners violated their own canons that they were able even to recognize the existence of the salient phenomena of our epoch. It remains to put Marx's system to the same test.

Professor Böhm-Bawerk, Minister of Finance to His Imperial Highness the Emperor of Austria, writing in the high noon-tide of capitalism (in 1896) had no doubt of what the results of such a test would be. Marx's system, he wrote, “ is not in close touch with facts.”

“ Marx has not deduced from facts the fundamental principles of his system, either by means of a sound empiricism or a solid economico-psychological analysis ; but he founds it on no firmer ground than a formal dialectic. This is the great radical fault of the Marxian system at its birth ; from it all the rest necessarily springs. The system runs in one direction, facts go in another.”

In 1896 Marxism seemed to Böhm-Bawerk, the most serious and talented of its capitalist critics, to have no future. But in the event it was the Austrian Empire, the Emperor, his Minister of Finance, and the theoretical constructions by which the Minister explained the existence both of himself and of his Emperor, which had no future.

Marxism will have no future, Böhm-Bawerk continues, because its “ hollow dialectic ” will at length be exposed by “ facts and the secure linking of causes and effect.” But has it been found that Marxism withers if it is exposed to the influence of

other than those used by Marx.” The assumptions of modern equilibrium economics, on the contrary, “ prove ” that the breakdown of capitalism cannot, and that wars need not, occur. It is only, as we saw, by breaking through their own system of assumptions that modern capitalist economists are able to recognize the existence of such phenomena as capitalist crises at all.

These grave errors arise because Professor Hook has not himself seen the application of the labour theory of value. He should re-read pp. 250 to 300 of Vol. III of *Capital* and then reflect on whether Bukharin was so wrong, after all, in believing that the labour theory of value had enabled Marx to predict the conditions in which we now live.

facts, and to the maximum amount of open discussion and debate? It is singular that, although Marxism has gained in influence ever since Böhm-Bawerk wrote, until it is now the accepted basis of the culture of one-sixth of the world, and is the one growing and vital theory of the other five-sixths, no attempts of an equal seriousness to Böhm-Bawerk's own have subsequently been made to expose "its hollow dialectic." The theorists of capitalism have almost unanimously decided that it was the better course to leave Marxism alone.

But this is not to say that the most strenuous and desperate efforts are not being made by the capitalist class to combat Marxism. In Austria, in Germany, and in ever widening areas of the capitalist world to-day we are witnessing unprecedented attempts to kill Marxism. But these attempts are not being made by Böhm-Bawerk's method of careful study and criticism. They are being conducted by means of the prohibition under pain of death and torture of all discussion of Marxism. To-day Böhm-Bawerk's successors in the seats both of the Austrian Government and of the European Universities have discovered that open discussion, that a rigorous comparison of Marxist theory with the facts, serve only to strengthen Marxism a hundred times. Accordingly Marxism is to-day a proscribed doctrine in most of Europe. How splendid a tribute to the truth of Marxism is that proscription! Is it necessary to proscribe "empty tautologies"? Need men be beaten to death for studying futile and insignificant abstractions? We cannot believe it so. Marxism is proscribed in a growing part of the capitalist world to-day, not because it "goes in one direction and the facts go in another." Marxism is proscribed, the methods of the Holy Inquisition are revived for its attempted extirpation, because it corresponds to the contemporary facts of the capitalist world with all too deadly an accuracy.

The future of Marxism, which Böhm-Bawerk could not foresee, is to show men why and how their present form of civilization is falling into an ever more bloody decay, and in what manner they may rebuild civilization on a new and higher basis. In five-sixths of the world Marxism is accomplishing this task: in one-sixth of the world this task is already upon the road to full accomplishment.

## “THE GREAT CONTRADICTION”

### SUMMARY OF CHAPTER XV

“The Great Contradiction” stated. According to Marx’s theory the rate of profit must vary with the proportion of variable to constant capital. But it does not. The rate of profit is constant throughout the productive system. Marx’s solution. The amount of profit made by a firm, in the sense of actually extracted in the process of production, is not kept by that firm. It is pooled with all the profit made by all the other firms : then each firm draws the amount of profit which will give it an average return on its capital out of this pool. This means that commodities sell at their prices of production, *i.e.*, at their cost of production plus a sum which will give an average return on the capital used in making them. Marx’s solution complete. But it involves the admission that commodities do not even tend to sell at their value. They tend to sell at their prices of production. And these prices of production are above their values if they are produced by a firm using little variable and much constant capital, and below their value if they are produced by a firm using much variable and little constant capital.

What connection, then, has the concept value, as determined by socially necessary labour time, with the “real phenomena of production”? It follows from the above that commodities which happen to be produced by firms using a capital of average composition do tend to sell at their value. But all the commodities produced by society must be produced by a capital of average composition. For clearly the total social capital must have a particular composition, one particular proportion of constant to variable capital, in it at any one time. We know this because this proportion slowly changes. Hence all the commodities produced by society must sell at their value. The total prices of all commodities add up to their total values. The sum total of commodities is made up of units of socially necessary labour time. Prices represent, though for particular commodities imperfectly, units of socially necessary labour time.

But unless we realize that prices represent real quantities—that they are the money names for real quantities—a total of prices is meaningless. And, as Professor Robbins wrote, for capitalist economists, prices do not represent real quantities at all. They

merely express the exchange ratio of commodities. And you cannot have a total of ratios. Böhm-Bawerk's emphasis of this point. Böhm-Bawerk reveals his conception of the nature of economic science. He wishes that Marx had been a marginal utility economist. The two incommensurable structures of economic thought. Which is relevant to reality? Which enables us to comprehend the present and to predict the future? This is the decisive test. We have already submitted capitalist economics to this test; and we have seen that it does not survive it. In the next Part we shall apply the same test to Marx's theoretical system. Böhm-Bawerk in 1896 had no doubts as to the result of such a test. He considered that Marxism was out of touch with facts and so had no future. But it was Böhm-Bawerk, his Empire, his Emperor, and his theories, which had no future. He believed that Marxism would die when it was exposed to careful refutation. But no considerable effort at refutation after his has been made. Instead, Marxism has been proscribed. The tribute of that proscription. Why torture men for studying insignificant abstractions? Marxism proscribed because it accounts all too accurately for the facts of capitalist decay. The future of Marxism is to teach men to comprehend the present and to control the future.



**PART IV**

**MARX'S THEORY OF  
CAPITALIST CRISIS**



## CHAPTER XVI

### *The Two-Faced Law*

WE have come at last to the crux of our enquiry. We have seen that the labour theory of value is not an empty abstraction. We have claimed that the structure of thought which Marx reared upon that theory will, unlike contemporary capitalist economics, stand the test of an application to the observed facts of our everyday life. We have claimed that Marxian economics will both explain the present condition and make it possible to predict the future destiny of the capitalist system.

We pass immediately to this decisive test. We shall apply the hypothesis that value is determined by socially necessary labour time to the problem of the nature of capitalist crisis. We shall submit that this hypothesis, and this hypothesis alone, makes possible an adequate explanation of why and how crises occur. The labour theory of value and the categories based upon it make it possible for us to understand what capitalist crises are, why and how they arise, and how particular crises have been overcome.

When we have accomplished this elucidation we shall be in a position to make rational and significant predictions as to whether further crises will occur and, if so, what will be their nature, their degree of severity, and their consequences. In fine, the labour theory of value, and the constructions based upon it will enable us to answer those questions which we posed in Chapter I.

The elucidation of the nature of capitalist crisis is the task for which Marx used the labour theory of value in the third volume of *Capital*. This elucidation is accomplished in Part III of the volume, which follows immediately upon the discussion of "the great contradiction." That discussion, we recall, led to a demonstration that the total value of the commodities produced by a given capitalist economy, although not the relative prices of particular commodities, is determined by the amount of socially necessary labour time expended in their production. Part III is called "The Law of the Falling Tendency of the Rate of Profit." The exposition and elucidation of this law is a most important application of the labour theory of value.

It will at once become evident to the reader that a tendency of the rate of profit to fall is a necessary corollary of the view that value is produced by living labour alone. We know that as the technique of production develops less and less living labour and more and more plant and machinery is used to produce a given quantity of products. Therefore in the production of a given quantity of products or in the use of a given quantity of capital equipment, less and less value must be created. And if less value is created, less surplus value also will be created. For surplus value is simply the capitalists' share of value in general. And the capitalists will hardly be able to increase their share of value sufficiently to compensate them for any serious falling off in the total amount of value created. Thus we see that a tendency for the amount of surplus value or profit (for taking the productive system as a whole they are the same thing) which the capitalists can get hold of from the production of a given supply of commodities, or the use of a given amount of capital, must, on this view of things, be continually tending to decrease.

We must state the point much more precisely than this, however. Since living labour alone creates value, surplus value or profit can be created by the variable capital, by that portion, that is to say, of capital which is used to employ living labour, alone. Hence, if the rate at which the variable capital produces profit remains the same, the amount of profit will depend simply on the amount of the variable capital. For example, if the whole economic system uses £1,000,000 of variable capital and the rate of surplus value is 100 per cent, the *amount* of profit will be £1,000,000. But the average *rate* of profit will depend on how big is the total capital of the system. For it is with the total capital of the system that you have to compare this amount in order to find the rate of profit. For example, if, with a variable capital of £1,000,000, the constant capital which the whole system employs is £3,000,000, then the total capital is £4,000,000. In that case, £1,000,000 of profit means a rate of profit of 25 per cent. But, if the system has to employ a constant capital of £9,000,000 in order to get its £1,000,000 of profit, the total capital will be £10,000,000. Then this same amount of profit of £1,000,000 will only mean a rate of profit

of 10 per cent. Thus it is clear that a growth of the constant capital in proportion to the variable capital used by the whole system must mean, other things being equal, a decline in the rate of profit. But a growth of the constant capital in proportion to the variable capital is only a novel way of expressing the development of the technique of production. And nothing is more certain than that the technique of production has become more and more developed during the whole history of capitalism, and that to-day it is developing at an unequalled rate.

Hence there has been, and there is, a powerful factor tending continually to depress the rate of profit. Here, stated in the broadest possible way, is the law of the tendency of the falling rate of profit.

In order, however, to elucidate the full consequences of this law, the reader will perhaps permit us to use a little shorthand. We wish to write this phrase, "the proportion of variable capital to constant capital," as  $\frac{v}{c}$ . The  $v$  stands for variable capital, the  $c$  stands for constant capital. Marx uses a big  $C$  when he means the total capital, and a small  $c$  when he means the constant capital, and we will follow his example. Putting one letter over the other, the  $v$  over the  $c$ , thus  $\frac{v}{c}$  means that one is divided by the other. When we write that " $\frac{v}{c}$  falls," we mean that the proportion of variable to constant capital falls. For example, we shall write the conclusion that the rate of profit depends predominantly on the proportion of the variable to the constant capital by the phrase "the rate of profit depends predominantly on the magnitude of  $\frac{v}{c}$ ." We shall have to use this conception of the proportion of variable to constant capital so often that our text would become almost intolerably cumbrous if this piece of shorthand were not allowed.

This conclusion that the rate of profit depends, other things being equal, on the magnitude of  $\frac{v}{c}$  is of the first importance. For the fall of  $\frac{v}{c}$  has been, and is, of so continuous and considerable a character that "other things" *have been*, comparatively speaking, equal. In other words, the fall of  $\frac{v}{c}$  has been, and is, so great as to dominate the situation and to produce in actual practice a continual tendency to depress the rate of profit.

Now the main "other factor" in the determination of the rate of profit is clearly the rate of surplus value. We may put

it like this : the rate of profit will depend upon how many pounds of variable capital producing surplus value are contained in the total capital, and on how much surplus value each of these pounds of variable capital is producing. Hence a sufficiently large rise in the rate of surplus value could offset a sufficiently small fall in  $\bar{v}$ . And, in fact, we find that the same causes which have led all through the history of capitalism to a fall in  $\bar{v}$  have also led to a rise in the rate of surplus value. But, for reasons which we shall discuss in the next chapter, this rise in the rate of surplus value has never been, and can never be, sufficient to offset fully the fall in  $\bar{v}$ .<sup>1</sup>

We can now express the main practical conclusion of the argument more exactly. If the rate of profit depends predominantly upon the magnitude of  $\bar{v}$ , then the rate of profit must in actual practice tend continuously to fall. For there is not the slightest doubt that the proportion of variable to constant capital has fallen, is falling, and must continue to fall. For this fall is the very essence of technical progress.<sup>2</sup>

This is how Marx puts the point. The fall in  $\bar{v}$ , he writes, is "but an expression of the progressive development of the productive powers of society, which is manifested by the fact that the same number of labourers, in the same time, convert an ever growing quantity of raw and auxiliary materials into products, thanks to the growing application of machinery and fixed capital in general, so that less labour is needed for the production of the same, or of more, commodities." (*Capital*, Vol. III, p. 248.) A vital application of the Marxian categories of economic discourse is, then, to show why it is that the rate of profit must continually tend to decline as production becomes more and more technically developed—as, in other words, the capitalist system itself develops.

The reader may feel that the complex system of hypotheses,

<sup>1</sup> Indeed, as we have already suggested, it is on the face of it unlikely that the capitalists could increase their share of the total value created sufficiently to offset any large or long continued fall in the amount of it produced per pound of total capital. For, after all, the workers have to be left something to live on.

<sup>2</sup> We are just beginning to experience the attempt to set up under fascist auspices a technically non-progressive capitalist economy. But for reasons which we shall see later this is an impossibility. It is true that capitalist states under fascist management, if they were left long in existence, would end technical progress. But they could only do so by ending civilization itself in a welter of wars.

springing from the conception of value as socially necessary labour time, which we have expounded in the two preceding chapters, is but a tenuous basis for this weighty conclusion. But we must recollect that the *fact* of an ever present tendency for the rate of profit to decline is widely admitted. Our empirical investigations in Part I of this book, at a stage in the argument when we had never heard of the labour theory of value, led us straight to the conclusion that a crisis was a collapse in the rate of profit. A sudden loss of profitability throughout industry was how Professor Robbins, for example, defined a crisis. There is no doubt that the system is subject to periodic collapses of the rate of profit. Additional evidence of this is afforded by the fact that all the remedial measures of the capitalist economists turned out to be nothing else but alternative methods of applying artificial respiration to the rate of profit. Thus the fall of the rate of profit as an observed fact of experience is hardly in question.<sup>1</sup> What we are trying to do is not to prove the existence of this fact, which is only too painfully evident, but to arrive at an understanding of it. For we found that no adequate explanation of it was forthcoming from any capitalist authority. (It is true that Dr. Hayek recognized its existence and its definite correlation with the extent to which production becomes technically developed—the extent to which the structure of production is lengthened, or production becomes more round-about, as he would say. For these are still other names for the phenomenon which Marx refers to as the fall of  $\bar{y}$ . But we were offered no explanation of why this process affects the rate of profit.)

We see, then, that what the Marxian categories of economic discourse have offered us is a rational explanation of why it is that the rate of profit falls, that fall itself being an observed fact. Moreover, as we shall now show, they enable us to understand the otherwise inexplicable measures which the capitalists take in order to offset, if they can, the perpetual tendency of the rate of profit to sag. They allow us to appreciate the necessity for those repeated applications of artificial respiration to the rate

<sup>1</sup> This fall does not take place evenly or smoothly, but in a series of jerks, which are the cyclical crises. The rate of profit is maintained for a period without decline and then suddenly collapses. We shall discuss the reasons why the law manifests itself in this uneven, jerky way in succeeding chapters. (Dr. Hayek has already given us some insight into this phenomenon.)

of profit which, since they involved attempting to cure a glut by cutting down everybody's purchasing power, we found so paradoxical. (See Chapter VII.)

We have so far established the fact that the growth of the productive power of society, that "economic progress" in general, is inseparably linked with a tendency to a falling rate of profit. The next point to take up is the question of whether this matters. Is or is not a falling rate of profit compatible with the health of capitalism? Is there any reason why capitalism should not be able to function efficiently even with a falling rate of profit? This faces us squarely with the question of what is the object of capitalist production. The answer, we already know, is profit. This is agreed by every authority from Professor Robbins to Marx. In the last resort what matters to the capitalist class as a whole is the *amount* (and not the rate) of profit which they can make. It is in order to obtain the maximum amount of profit that they carry on production.<sup>1</sup> Does not this at once suggest to us a way in which the capitalist class may compensate itself for a falling rate of profit? The rate of profit is falling, we recollect, because of the fall of  $\frac{v}{c}$ . But  $\frac{v}{c}$ , the proportion of variable to constant capital, may be falling either because the amount of  $v$  is falling or because the amount of  $c$  is rising. Indeed, it is evident that the amount of  $v$  may actually be rising, but yet  $\frac{v}{c}$  may fall, if  $c$  is rising faster than  $v$ . In other words, the proportion of the two parts of capital tells us nothing about the size of the total capital. And it is on the total capital, we know, that the rate of profit is calculated.

We see at once that if the total capital is growing fast enough, a falling *rate* of profit may not prevent the successful accumulation of an ever growing *amount* of profit. For example, let us say that  $v$ , the variable capital, of a given community rises from £2,000,000 to £3,000,000,<sup>2</sup> and that at the same time its constant capital rises from £4,000,000 to £15,000,000. Thus the community's total capital rises from £6,000,000 to £18,000,000. But

<sup>1</sup> What matters to the individual capitalist *per contra* is the rate of profit on his capital which he can make. For this alone guides his choice as to how he will use his capital.

<sup>2</sup> The reader may put in noughts to taste, in order to make a more realistic illustration of the total capital of a modern capitalist state.



at the same time  $\frac{v}{c}$  has dropped from  $\frac{1}{2}$  to  $\frac{1}{3}$ . In these circumstances the *amount* of profit made will rise (always on our old assumption of a constant rate of surplus value of 100 per cent) from £2,000,000 to £3,000,000. But the rate of profit is the amount of profit compared to the total capital. It was therefore £2,000,000 compared to £6,000,000, or  $33\frac{1}{3}$  per cent. Now it has become £3,000,000 compared to £18,000,000, or  $16\frac{2}{3}$  per cent. *So, even though the amount of profit has gone up by 50 per cent, the rate of profit has gone down by 50 per cent.* We begin to see the capitalist solution of the problem. The capitalists can find a compensation for the ever falling rate of profit in an ever growing amount of profit, secured by an ever growing total capital.

See, however, what this involves. In order that the amount of profit may grow, in spite of the falling rate of profit, *the total capital must grow fast enough to more than offset the falling proportion of  $v$  to  $c$ .* In other words,  $v$ , the variable capital, must actually grow in absolute magnitude, in spite of the inevitable fall in its magnitude relative to  $c$ , the constant capital. Thus in our example  $v$  grew from £2,000,000 to £3,000,000. But this, in view of the fall in  $\frac{v}{c}$  from  $\frac{1}{2}$  to  $\frac{1}{3}$ , was only possible because of the far faster growth of  $c$ , from £4,000,000 to £15,000,000. It is clear that, if this kind of situation can be achieved, all will be well. The amount of profit will grow, and so the capitalists will have an incentive to go on producing goods and employing labour on a larger and larger scale. For it is the amount, and not the rate, of profit, we repeat, which matters to the capitalist class as a whole. It will pay the capitalists, that is to say, to go on increasing the total capital of the community so long as doing so yields them an increased amount of profit. It will pay them to do so even though the increase in the amount of profit is not proportionate to the growth of the total capital, even though they obtain a continually falling rate of profit on their continually growing total capital. Here is how Marx sums up the way in which the capitalist system may carry on in spite of a falling rate of profit.

“ We see, then, that in spite of the progressive fall of the rate of profit, there may be an absolute increase of the number of labourers employed by capital, an absolute increase of the

labour set in motion by it, an absolute increase of the mass of surplus labour absorbed, a resulting absolute increase of the produced surplus value and consequently a resulting absolute increase of the mass of the produced profit. And this increase may be progressive. And it *may* not only be so. On the basis of capitalist production, it *must* be so, aside from temporary fluctuations.

“The capitalist process of production is essentially a process of accumulation.” (*Capital*, Vol. III, chap. xiii, p. 255.)

The last sentence of this passage is worth noticing. Marx is emphasizing that the happy result of increased profit and increased employment, which, he has shown, can be achieved in spite of a falling rate of profit, can be achieved by means of a sufficiently rapid growth of the total capital alone: that is, by a sufficiently rapid accumulation alone. For think what would happen if the total capital of £6,000,000 in our example had only grown to £8,000,000 instead of to £18,000,000, while  $\frac{y}{x}$  was falling from  $\frac{1}{2}$  to  $\frac{1}{3}$ . With a total capital of £8,000,000, we should then have had £1,600,000 of variable capital and £6,400,000 of constant capital. The amount of profit would have dropped from £2,000,000 to £1,600,000. In spite of the growth of the total capital from £6,000,000 to £8,000,000, the profit would have dropped by £400,000. The amount of profit would have been much less after the process of accumulation than it was before it. The capitalists would have had no inducement to go on producing or accumulating. On the contrary, they would have lost £400,000 of profit by having accumulated an extra £2,000,000 of capital. Under such circumstances the system would immediately cease to function. This is what Marx means by saying that “the capitalist process of production is essentially a process of accumulation.”

*In order that capitalism should continue to function at all, an extremely rapid accumulation, a rapid growth of the total capital must take place. Otherwise the machine runs down.* Every penny of profit which the capitalists can make is urgently needed by them for the purpose of adding it to their total capital. For it is only by means of a sufficiently rapid increase in their total capital that the effect upon profits of the continuous fall in  $\frac{y}{x}$

can be compensated. It is essential for them, as Marx puts it, "that the mass of surplus value, and of profit, appropriated by them should grow simultaneously with the fall of the rate of profit, and in spite of it." And this they can only accomplish by accumulating, by increasing their capital so fast that its growth in total amount more than compensates for the decline in the rate of profit which each pound of it yields. Marx, basing his argument on the fact that capitalism had continued to function, writes of this necessity to accumulate fast enough to offset the fall in  $\bar{v}$ , and the consequential fall in the rate of profit, as a "law." He writes of it, that is to say, not as something which the capitalists have to try to accomplish, but as something which they actually do accomplish. ("And it *may* not only be so. On the basis of capitalist production, it *must* be so.") Indeed, it is evident that, so long as capitalism is in existence, this rate of accumulation is a law: it is a law of capitalism. It is something which the mere continued existence of the system proves to be in operation. For it is only by the fulfilment of this law that the system can continue to exist.

This is what Marx calls "the two-faced law": two-faced because it decrees that *both* a falling rate of profit *and* a rising amount of profit are conditions necessary to the existence of capitalism. We have seen that these two conditions can only be simultaneously fulfilled by a sufficiently rapid accumulation of total capital.

Now all this can be expressed in terms of employment instead of in terms of profit. Instead of saying that the total capital must increase fast enough to more than offset the fall in  $\bar{v}$ , for only so can the amount of profit be increased, we can say that the total capital must grow at this rate in order to increase the amount of employment offered. In either case the crux of the matter is to achieve an increase in the absolute magnitude of  $v$ , the variable capital. For on the magnitude of  $v$  depends not only the amount of profit, but also, and even more directly, the amount of employment. Evidently it is only if  $v$ , the amount of capital devoted to paying wages, grows, that more employment can be given.<sup>1</sup> But this way of looking at the problem in terms of

<sup>1</sup> Unless, of course, wages are reduced. We consider this eventuality below.

employment is more complicated, since we must here take into consideration the growth of the labouring population. Let us say that the total capital is growing more than enough to offset the fall of  $\bar{y}$ , and thus to produce an increasing amount of profit. In this case the absolute magnitude of  $v$ , the wage paying capital, must be growing. But it will not necessarily be growing as fast as the labouring population is growing. In other words, all the conditions for the continuance of capitalist production may be fulfilled and yet there may be an ever growing army of unemployed. Indeed, Marx writes, there *must* exist, if not an ever growing, yet a permanent and substantial army of unemployed. This is itself another condition of the continued working of capitalism. For if the total capital grew so rapidly that  $v$  not only increased, but increased faster than the growth in the working population, new and most formidable difficulties would beset the system. We shall explain the nature of these difficulties below. Marx, however, considered that this was a hypothetical question. He did not, at any rate, think that these particular difficulties had ever arisen up till the time at which he wrote.

We can now calculate how fast must be the rate of accumulation of the total capital. It must be fast enough to make  $v$ , the variable capital, grow. It must, in other words, be fast enough to a little more than offset the fall of  $\bar{y}$ . Hence the rate of accumulation necessary for the system is governed by the rate of the fall of  $\bar{y}$ . If  $\bar{y}$  is only falling slowly, then quite a moderate growth of the total capital will serve to offset it and produce some increase in the total size of  $v$ , and so in the amount of profit and employment. But if  $\bar{y}$  is falling more and more rapidly, then only a more and more rapid growth in the total capital will do. (And a fall of  $\bar{y}$  means, let us recollect, "mechanization," "rationalization," "improved technique," "economic progress," call it what you will.)

Marx supplies a formula for this necessary minimum rate of accumulation which must be attained unless the amount of profit is to decline and the system to stall.

"In order that the mass of profit made at a declining rate of profit may remain the same as before, the multiplier

indicating the growth of the total capital must be equal to the divisor indicating the fall of the rate of profit." (*Capital*, Vol. III, p. 260).

This is easy to see if the point is exemplified. Say that each year the rate of profit is halved (not, of course, that the rate of profit ever falls anything like so fast as this). The first year a capital of £100 will give £40 or 40 per cent, the next year £20 or 20 per cent, the next year £10 or 10 per cent, the next year £5 or 5 per cent. In these circumstances it is clear that in order that the amount of profit should remain the same, the total capital must double each year. The second year the total capital must become £200 in order to give £40 at 20 per cent, the third year the capital must grow to £400 in order to give £40 at 10 per cent, the fourth year it must have grown to £800 in order to give £40 at 5 per cent. In this case "the multiplier indicating the growth of the total capital and the divisor indicating the fall of the rate of profit" are both 2. But, Marx writes, accumulation must be just a little faster than this. It must be at least fast enough to make the amount of profit not only stay the same, but grow a little from year to year, in spite of the fall in the rate of profit. For otherwise there will be no incentive for the capitalists in the whole business of accumulation.

This is the formula of the minimum rate of accumulation necessary to capitalism. If ever, and whenever, the rate of accumulation falls below this level, the system must, and does, jam. For it becomes more profitable for the capitalists to restrict than to expand production. And, unless it pays the capitalists better to use more capital and give more employment, they will use less capital and give less employment. Nor is this due to original sin on their part. They cannot possibly help themselves. Each and every capitalist must, on pain of ceasing to be a capitalist, seek to make the most profit and the least loss. No one can undertake the risks of laying out an additional sum of capital, and giving an additional amount of employment, unless it pays him better to do so than to leave this additional capital idle and carry on on the old scale of production.

We have established the fact that there exists for any capitalist economy a certain minimum rate of accumulation, a certain

minimum speed, that is to say, at which its total capital must grow if the system is to function. And we have established the fact that this minimum rate of accumulation is determined by the speed at which  $\frac{v}{c}$  is falling; by the speed, that is to say, of technical progress.

This is a conclusion of the utmost importance. For it, and it alone, enables us to understand why it is that it is impossible to solve the fundamental difficulty, the basic and ever recurrent crisis of capitalism, in the simple way advocated by all reformers. The essence of every capitalist crisis is, in spite of the paradoxes of the professional capitalist economists, that the population is unable to purchase, and so consume, the ever growing quantity of consumers' commodities which come pouring on to the market. The essence of every crisis is, visibly and obviously, a glut. No one who has ever lived through a great capitalist crisis, such as that of 1929, can possibly doubt this fact. Why, then, say the reformers, cannot this glut be cured by the simple and obvious expedient of "distributing purchasing power"? How can it be maintained that "a policy of high wages" combined, if necessary, with the institution of social services, such as pensions and insurances, would not solve the problem by giving everybody the money to buy the available goods, and so end the glut? At length we can say clearly why this policy cannot be adopted. It cannot be adopted because to raise wages, or to increase taxation in order to pay for social services, would at once begin to diminish the rate of accumulation: it would make it impossible for the capitalists to augment their total capital at a pace sufficient to offset the fall in  $\frac{v}{c}$ , and so achieve that indispensable purpose, some growth in the absolute magnitude of  $v$ .

It is clear, moreover, that it is just precisely to-day, when technical progress is proceeding at an unequalled rate, when the bottom is dropping out of  $\frac{v}{c}$ , that every available penny must be devoted to accumulation. And this is why, as we have already seen, the capitalists in actual practice, far from trying to cure the recurrent gluts of the system by increasing the non-capitalists' purchasing power, apply the paradoxical remedy of reducing everybody's purchasing power either by cutting wages or raising prices. (Indeed, we saw that the whole dispute between

the different schools of capitalist economists turned out to be concerned exclusively with the question of which of these methods of reducing purchasing power should be adopted.)

For we can now see that any increase in wages, that, indeed, any failure to cut wages, while it would help to dispose of the glut of consumers' commodities, would do far more harm than good to the capitalists' system. For wages (and money for social services) have to be taken from the only funds which are available for accumulation. Hence if they are not rigorously kept down to the necessary minimum, accumulation will be checked; the total capital will not grow sufficiently to offset the fall of  $\bar{y}$ ; the absolute magnitude of  $v$  will fail to grow, or will actually shrink. But yet if wages and social services are kept down to a minimum, how is the glut of consumers' commodities to be disposed of?

Here, then, is the fundamental dilemma of capitalism, which we called in Part I the dilemma of profits or plenty. Now, however, we are enabled by Marx's analysis to describe the situation far more clearly and accurately. If wages and social services are kept down to the necessary minimum, the familiar crisis of glut must occur.<sup>1</sup> But wages and social services cannot be raised; for to do so would be to depress the rate of accumulation to a level at which it could no longer offset the fall of  $\bar{y}$ . It is the existence of this dilemma which makes capitalist crises inevitable. We shall devote most of the rest of this Part to showing how capitalism swings desperately between its horns.

We now see just why Professor Robbins, Dr. Hayek, and their school prescribed the maximization at all costs of the rate of accumulation, or of the rate of saving, as they called it, as the specific for the healthy functioning of capitalism. They pointed out that the one way in which this could be achieved was by as uneven a distribution of wealth as possible: by a pinning down of wages to their "economic level": by a curtailment, or, if possible, abolition, of social services, and the consequent repeal of taxation on the accumulations of the rich. We shall discuss in subsequent chapters the extraordinary nature of the "solution" to which this line of argument must lead. But already it is

<sup>1</sup> We deal with the Hayek-Robbins' denial of this necessity below.

evident that capitalism is a very different system either from what it appears to be to the casual observer, or from what most of its own theorists describe.

We see that capitalism can only work if the mass of the population is kept down to a subsistence level and every possible penny of new value is accumulated, is turned, that is to say, into capital, and used—and used for what? For the production of still more capital. Again we see the vision of capitalism rushing off into infinity. Again we see that vision of progression at the rate of compound interest which so astonished Mr. Stuart Chase, Mr. Basset Jones, and other American statisticians. Again we see the vision of the whole earth being covered with means of production, and with means of production of means of production, and with means of production of means of production of means of production. “What, will the line stretch out to crack of doom?” we may well enquire. Nor will our astonishment be diminished when we observe that the very condition of this infinite creation of means of production is that only the very minimum of actual production, of the production of actual consumable use values, that is to say, should be undertaken.

Again, we see that capitalism, like the Red Queen in *Alice*, has to run faster and faster even to stay in the same place. The total capital must grow faster and faster in order to offset the ever accelerating fall of  $v$ . Only so can the magnitude of  $v$ , on which depends the amount of profit and employment, be prevented from actually diminishing. And to make  $v$  grow, capitalism must run, or accumulate, faster still. Hence the ever more desperate cries of Dr. Hayek, Professor Robbins, and those of capitalism’s theorists who have any understanding of the situation. Hence their horror at any proposals which aim at curing a glut of consumers’ commodities by drawing on the funds available for accumulation. “Faster, faster,” they urge. The capitalists must save and accumulate every penny they can, for the demon of the ever falling amount of profit and employment which any given pound of capital can provide is at their heels. And ever more desperately the capitalists do strive to accumulate. Ever more recklessly they strive to speed up their system, by cutting wages, slashing social services, by wringing every



possible penny of profit from the workers. Individually they must do so in order to survive in their internecine competitive struggle. As a class they must do so in order to prevent the nemesis of the falling rate of profit from overtaking them.

Here, then, we have run to earth the devil in capitalism. Here we have discovered what it is that drives the system relentlessly on. It is this which prevents the system from solving its periodic gluts by increasing mass purchasing power. It is of the very essence of capitalism that there can never be a period of "stabilization" in which we can enjoy the fruits of our past labours. Under capitalism we can never use our gigantic means of production for any purpose but the creation of further means of production. Any substantial attempt to increase the purchasing power of the population sufficiently to allow them to secure more than a minimum supply of consumers' commodities must at once destroy the system.

To-day the quintessentially accumulative nature of capitalism makes that system an insane monstrosity. In the past, however, it was this very characteristic which carried the system forward in triumph. There was a time when the dynamic principle contained in the falling tendency of the rate of profit served a mighty historical purpose. The "two-faced law" decreed that that very technical progress which first increased each capitalist's profits, next reduced the rate of profit of all of them, and so drove them all to compensate themselves by means of augmenting their total capital at the maximum possible rate of accumulation, in order that, in spite of everything, they might increase their amount of profit. This was the law which industrialized half the world. This was the law that launched not only a thousand ships, but built tens of thousands of factories, sunk innumerable mines, drained marshes, and built cities. Marx again and again points out the historic function which capitalism and the capitalists performed in thus developing, with savage and ruthless vigour, but in the only way in which they could be developed, the long-dormant productive powers of the race. He twice calls the capitalists "the trustees of society." They were the men into whose hands the vast new wealth created by the unleashed powers of social production necessarily and inevitably flowed. (But Marx never forgot to add that the capitalists were

always the uncontrolled, and were often the fraudulent, trustees of society.)

To-day the two-faced law has done its work. Once the task of putting men's productive powers upon a new basis, upon the basis of mechanical power instead of muscle power, had been accomplished, the falling tendency of the rate of profit began to close in upon the system. Unmercifully this law of their system's very nature drove, and drives, the capitalists to turn this way and that for a way of escape from its remorseless pressure. It is this law which drives them to maximize their accumulations even at the cost of producing intolerable conditions for the overwhelming majority of the population. It is this law which compels them to keep wages at the lowest possible level : to starve, if they can, the ever growing army of the unemployed so that they may be driven back into the factories, even at below a true subsistence level of wages : it is this law which drives them to wring the last anna of rent or of usury from the ryot of India, the last cent from the Chinese coolie. Above all, it is this law which drives them, however fearful and reluctant they may be, to attack each other for the right to use the few remaining opportunities of sustaining the rate of profit.

For this same two-faced law has become, above all, a law of war. Two-faced is Janus-faced : the temple of the two-faced god was a temple of war. The two-faced law of the falling rate of profit is a law of war. Its remorseless pressure drives the modern capitalists to the ends of the earth in search of regions where the rate of profit has not yet fallen so disastrously as at home. But they find there not only the helpless natives, but their own formidable rivals. For each national group of capitalists is hard pressed. Everywhere the same uncomprehended law is driving them to pile Pelion upon Ossa, hoping to bury beneath the mass of their capital the inescapable fact that every pound of it produces less and less profit. For the loins of capital in the old, developed capitalist states are becoming barren. Capital is becoming, as Marx would have said, less and less "organic." Each pound of it produces a smaller and smaller annual increment. Only the exploitation of some new untouched country, where modern mechanized methods of production have not yet been established, where the whole cycle of capitalist development

can be begun anew, can temporarily save the situation. And *who* is to save himself by developing those few remaining areas in which capitalism can renew its youth? *Who* is to perish for want of these remaining opportunities of salvation? These are life and death issues for each and every national group of capitalists to-day. They cannot be settled except by a life and death struggle.

## SUMMARY OF CHAPTER XVI

We apply the hypothesis that value is determined by socially necessary labour time to the problem of capitalist crisis. A tendency for the rate of profit to fall, inherent in the conclusions of the last chapter. For the rate of profit was seen to depend predominantly on the proportion of variable to constant capital. And this proportion is continually declining. The other determinant of the rate of profit is the rate of surplus value. But it is apparent that a rise in the capitalists' share in value cannot permanently offset a fall in the total quantity of value created.

A tendency for the rate of profit to fall, an observed fact. The point of Marx's analysis is that it alone enables us to account for this fact.

Does the falling tendency of the rate of profit matter? Under what conditions is it compatible with the existence of capitalism? The object of capitalist production is to increase the amount of profit. This object can be achieved in spite of a falling rate of profit if the total amount of capital can be increased sufficiently rapidly. The total capital must grow fast enough to offset the fall of  $\bar{p}$ . This is "the two-faced law" which lays it down that both a falling *rate* of profit and a rising *amount* of profit are necessary conditions for the existence of capitalism. All this can be expressed in terms of employment as well as in terms of profit. For employment depends even more directly than profit on the absolute size of  $v$ . For  $v$  is the only wage-paying capital. But  $v$  may be growing and yet unemployment may increase, for  $v$  may not be growing as fast as the working population. Marx supplies a formula for the minimum rate of accumulation necessary to capitalism. The total capital must grow fast enough to

cause the absolute magnitude of  $v$  to grow. Hence the necessary rate of accumulation depends on the rate of fall of  $\frac{v}{p}$ . If ever the rate of accumulation falls below this rate (a rate which will increase the size of  $v$ ), the system jams.

This conclusion enables us to understand the impossibility of curing capitalist crises by raising wages. We sight again the basic dilemma of capitalism. In Part I we called it the dilemma of profits or plenty. We can now describe it by saying that wages are at one and the same time so low that they cause a glut and so high that they diminish accumulation.

We can now fully comprehend the wage-cutting prescriptions of Dr. Hayek, Professor Robbins, and their school of capitalist economists. Their policy boiled down to a removal of all obstacles to a maximum rate of accumulation. Hence, although Marx alone can explain why this is so, it is agreed that a maximum rate of accumulation is the essential condition for the existence of capitalism. This is the devil within capitalism driving it onward. This is the law which industrialized the world. This is the law which is to-day driving the capitalists to seek ever new areas of exploitation. This is the law which is driving them to internecine conflict. The two-faced law has become a law of war.

## CHAPTER XVII

### *Counteracting Causes*

THE last chapter revealed the conditions necessary to the existence of capitalism. It showed the growing difficulty of fulfilling all these conditions simultaneously. If accumulation was maintained at a rate sufficiently rapid to offset the falling rate of profit, then it was difficult to see how enough money could be distributed to the population to avoid recurrent gluts of consumers' commodities. It is evident that the formidable difficulties with which contemporary capitalism is beset almost all arise from its necessity to accumulate at the maximum possible rate. It is this which makes it necessary for capitalism to adopt apparently paradoxical policies, such as reducing wages and social services in order to increase economic activity in a depression. It is this which drives it to cut down the purchasing power of the mass of consumers just when it is apparently in desperate need of a market. It is this which compels it to seek abroad those markets which the necessities of its own accumulative nature have driven it to destroy at home. And it is this which faces capitalism as a world system with the frightful prospect of ever more catastrophic wars as each and all of the great empires turn outwards for new markets.

It is the existence of the tendency of the rate of profit to fall which necessitates a hectic rate of accumulation. We have attained a far clearer comprehension of the contemporary situation of the world than is possible without a knowledge of the law of the tendency to a falling rate of profit. So far, however, we have found nothing predetermined about the outcome of that situation. It all depends upon the intensity of the pressure which the falling rate of profit exercises upon the system. There is no apparent reason why the system should not successfully adjust itself to a slowly falling rate of profit, for example. So long as the pressure is not too great we can envisage the possibility of further capitalist development without economic deadlock at

home and war abroad. How rapid, then, is the present tendency of the rate of profit to fall? When we observe the extreme degree of strain to which every national capitalism is, visibly, being subjected, and the even greater degree of strain which is, visibly, developing between each of them, we should expect to find, on investigation, that it is rapid. And so it is; for the steepness of that fall primarily depends upon the growth of the constant at the expense of the variable capital. And this is but an economist's phrase for technical progress.

To-day we cannot open a newspaper without being informed of the unparalleled acceleration of technical progress. A vast literature (often inaccurate and always ill-considered) exists on the rapidity with which modern productive methods are "saving labour." But what does "saving labour" mean? It means that no more, or even less, labour is being used each year to produce an ever growing total of products, by means of an ever growing quantity of constant capital. Therefore less value is being created relatively to the total physical volume of commodities produced and of capital used. The pool of value available for distribution to the capitalists and workers is consequently tending to get relatively smaller as compared to the capital which has to be laid out. Is it not obvious that there must be a continual tendency for the amount of value which the capitalists can get hold of to decrease relatively to the amount of capital which they have to lay down? And this *is* the tendency of the rate of profit to fall.

In our terminology,  $v$ , the variable capital, is being squeezed into a smaller and ever smaller part of the total capital. And this is going on everywhere, all the time, and at an unheard-of speed. There are, the technocrats delight to tell us, individual plants in which, so far as the actual productive process is concerned, the development has almost reached its logical conclusion. The product is not touched by human hand from start to finish.  $v$  has disappeared! (Or, rather, it has almost disappeared, for even the most automatic factory needs machine minders to take care of it.) In general, the pace at which the workers are being expelled from the factory is notoriously very rapid and is everywhere growing more and more rapid.

The American Federal Reserve Board has shown that output

per man-hour in terms of physical production in American industry has varied as follows :

January 1920 . . . . .	82
1923-25, average . . . . .	100
June 1929 . . . . .	123
March 1933 . . . . .	98
June 1933 . . . . .	142 <sup>1</sup>

Nor is this tendency confined to the United States. In technically conservative Britain, in the prudently managed Austin Motor Company of Birmingham, the figures of men employed per car manufactured have varied as follows :

1922 . . . . .	55
1927 . . . . .	11
1934 . . . . .	8 <sup>2</sup>

Such figures, it is notorious, could be multiplied indefinitely and could be shown to apply in a varying degree to every industrial country in the world. How fast, then, must accumulation go in order to offset a fall in  $\frac{1}{8}$  of this unheard-of rapidity ? How can it be possible for accumulation to be so rapid as to augment the amount of profit and employment in spite of a fall in the rate of profit of the rapidity indicated by this development ? Are we not in danger of having proved too much ? For, after all, though with unparalleled and ever increasing difficulty, the capitalist system has survived the catastrophic rapidity of technical progress during the last decade. Does it not look as if certain counterbalancing tendencies must exist which aid capitalism in its struggle with the falling rate of profit ? There are such tendencies. We must now begin to fill in the extremely schismatic outline of the last chapter by enumerating and evaluating, if we can, these counterbalancing forces.

It is interesting to notice that even fifty years ago Marx felt that once the main reason for the falling tendency of the rate of

<sup>1</sup> See Mr. Stuart Chase's article, "What Hope for the Jobless ?" in *Current History*, November 1933, for these and many more figures of the same kind.

<sup>2</sup> See *The Economist*, June 2nd, 1934. This is an excellent example of how the system can work if the rate of accumulation of capital is rapid enough. For, in spite of this catastrophic fall of  $\frac{1}{8}$ , the Austin Company has expanded its total capital so rapidly that the amount of employment which it has given has steadily grown. If ever, and whenever, capitalism as a whole can expand at this speed all is well with it.

profit had been grasped the difficulty was to account, not for the rapidity but for the comparative slowness of the fall. He begins the second chapter of Part III of Volume III with this very modern sounding passage :

“ If we consider the enormous development of the productive powers of labour, even comparing but the last 30 years with all former periods ; if we consider in particular the enormous mass of fixed capital, aside from machinery in the strict meaning of the term, passing into the process of social production as a whole, then the difficulty, which has hitherto troubled the vulgar economists, namely that of finding an explanation for the falling rate of profit, gives way to its opposite, namely to the question : How is it that this fall is not greater and more rapid ? There must be some counteracting influences at work, which thwart and annul the effects of this general law, leaving to it merely the character of a tendency. For this reason we have referred to the fall of the average rate of profit as a tendency to fall.” (*Capital*, Vol. III, chap. xiv, p. 272.)

We must turn to these counteracting influences immediately. The first of them is a tendency for the rate of surplus value to rise. We have demonstrated that the rate of profit depends upon the magnitude of  $\frac{v}{c}$ , *given a constant rate of surplus value*. In all our illustrative calculations we assumed a rate of surplus value of 100 per cent. But in fact the rate of surplus value will not be constant. It will rise, and it will rise for the very same cause, *viz.*, technical progress, or, as Marx more accurately calls it, the growing productivity of labour, which is depressing  $\frac{v}{c}$ . We have only to remember what the rate of surplus value is in order for this to become evident. The amount of surplus value produced in a given number of hours of work is determined by the amount of time which it takes a worker to produce enough value for himself and his dependants to live on : to produce the value, in other words, which he is paid in wages. For the amount of his wages, “ in equilibrium,” will be the amount necessary to enable him to live and to bring up a child with an equal degree of training and education to replace him.



Hence, of course, all technical improvements which reduce the value<sup>1</sup> of the necessities of life, reduce the value of labour power. If, by better agricultural methods, for example, it becomes possible to maintain 100 workers with 10,000 man-hours of agricultural work, instead of with 20,000, the value of the labour power of these labourers will be reduced correspondingly. The supply price of their labour in capitalist economist's language, will have been reduced. But this does not in itself mean that these workers will produce any less value. Let us say that 100 workers are producing £400 a week of value; that it costs them, and that they are paid accordingly, £200 a week to live (£2 a week each). (Thus the rate of surplus value is 100 per cent.) Now let us suppose that agricultural improvements make it possible for these workers to feed, clothe, and maintain themselves for £150 a week (30s. each). Their wages will fall to this level. (Unless the afore-mentioned "interferences" with capitalist equilibrium, such as trade unions and social services are in existence.) But they will still go on producing £400 worth of commodities a week. So now they will yield a surplus value of £250, and the rate of surplus value will become 188 per cent.

Here, then, is something that may greatly offset the fall in the rate of profit. And yet it is evidently very closely bound up with that very factor, technical progress, which is causing that fall. For it was, we said, "agricultural improvements" which made this increase in the rate of surplus value possible. But "agricultural improvements" are themselves but a particular instance of technical progress. Hence they mean a fall of  $\frac{1}{2}$  in the capital employed in agriculture. They mean that the rate of profit on agricultural capital is going down. And this must be depressing the general rate of profit. Hence technical improvement, the growing productivity of labour, acts in an opposite sense on the two determinants of the rate of profit. By causing the number of labourers employed by a given amount of capital to decline, it depresses the rate of profit. But by increasing the amount of value which can be taken from each remaining labourer, it raises the rate of profit. The question is which tendency will win? Marx is able to show that there is no doubt

<sup>1</sup> Which means, remember, the amount of socially necessary labour time needed to produce them.

that the increase in the rate of surplus value cannot do more than check the fall in the rate of profit. Here is his demonstration :

“ Now, surplus-value, as a total, is determined first by its rate, secondly by the mass of labour simultaneously employed at this rate, or what amounts to the same, by the magnitude of the variable capital. One of these factors, the rate of surplus-value, rises in one direction, the other factor, the number of labourers, falls in the opposite direction (relatively or absolutely). To the extent that the development of the productive power reduces the paid portion of the employed labour, it raises the surplus-value by raising its rate; but to the extent that it reduces the total mass of labour employed by a certain capital, it reduces the factor of numbers with which the rate of surplus-value is multiplied in order to calculate its mass. Two labourers, each working 12 hours daily, cannot produce the same mass of surplus-value as 24 labourers each working only 2 hours, even if they could live on air and did not have to work for themselves at all. In this respect, then, the compensation of<sup>1</sup> the reduction in the number of labourers by means of an intensification of exploitation has certain impassable limits. It may, for this reason, check the fall of the rate of profit, but cannot prevent it entirely.” (*Capital*, Vol. III, chap. xv, p. 290.)

Or look at it in this way. There must come a point at which the reduction of the amount of value produced per pound of total capital invested will reduce the capitalists' share of that value. For the reduced total value will drop below what was the capitalists' share. Hence that share (which is surplus value) would be reduced in size even if the capitalists could take all the value now produced.

We now come to a more subtle counteracting factor. We have spoken throughout of the fall of variable capital in proportion to constant capital, and we have meant throughout the fall of the value of the one compared to the value of the other. At the same time, however, we have said that the fall of  $\frac{v}{c}$  was but an unfamiliar way of expressing the platitude of

<sup>1</sup> “Of” seems very obscure here. Perhaps “for” would be a better translation.

technical progress. A qualification must now be introduced into this statement. Technical progress, taking the whole field of production, always necessitates the relative growth of the physical mass of the constant capital employed. But it does not necessitate a *proportionate growth* of the value of the constant capital. For technical progress is reducing the number of hours of socially necessary labour time which are necessary for the production of means of production as well as the number needed for the production of consumers' commodities. For this reason the value of the constant capital will not grow as rapidly as its physical volume. But, again, this can only check, not overcome, the fall of  $\gamma$ . For nothing is more certain than that the value, as well as the physical mass of the world's constant capital has grown and is growing enormously.<sup>1</sup>

The next counteracting influence is a special case of raising the rate of surplus value. There may be particular forms of technical change, Marx suggests, which raise the rate of surplus value without, at the same time, or to a lesser extent than normally, increasing the rate of fall of  $\gamma$ . He instances the prolongation of the working day as the leading example of this kind. Another example is an increased use of the three shift system, by which the same quantity of fixed capital can be used by a greatly increased number of workers.

Marx's next point is worth citation in full for the sake of the light which it throws upon all three volumes of *Capital*.

#### " II. *Depression of Wages Below their Value.*

" This is mentioned only empirically at this place, since it, like many other things, which might be enumerated here, has nothing to do with the general analysis of capital, but belongs in a presentation of competition, which is not given in this work. However, it is one of the most important causes checking the tendency of the rate of profit to fall." (*Capital*, Vol. III, chap. xiv, p. 276.)

<sup>1</sup> This, again, is the same point as that made by the technocrats, etc., when they talk of a gigantic growth of debt. " Debt " is our way of reckoning the value of the world's constant capital. But the technocrats' way of putting the matter is most misleading. They speak as if the world could have a net indebtedness to itself. They seem to ignore the obvious fact that every debit is somebody's credit. The total indebtedness of the world is always zero.

Here we see once more that the whole *quæsitum* of *Capital* is an analysis of capitalism in equilibrium. The whole of the forces analysed so elaborately by contemporary capitalist economists are assumed to be in operation by Marx. They are concerned with the attainment and preservation of equilibrium. Marx is concerned with whither equilibrium will take us. The capitalist economists are concerned to show how the fluctuations of supply and demand determine prices. Marx is concerned to show what is the meaning of the category "price." He is intent to show, not how and why price fluctuates, *but what it is that fluctuates*.

Marx's next substantial cause, counteracting the fall of the rate of profits, is foreign trade. Marx first considers the matter from the point of view of the export and import of commodities, without the export and import of capital. In general he shows that the primary effect of such trade is to check the fall in the rate of profit. For foreign trade will raise the rate of surplus value. It will do so by making possible the import of cheap food and necessities of life, thus lowering the value (subsistence rate) of wages. Marx was probably thinking of the greatest and most successful of all measures for the support of the rate of profit, namely the repeal of the Corn Laws by the British capitalists in 1846. This great *coup* drastically cheapened the necessities of life, and so made possible a general reduction in money wages. This enabled the British capitalists to raise the rate of surplus value and so do much to offset the fall of  $\bar{x}$  for the rest of the century.

But this, continues Marx, is only the first, short run, effect of foreign trade. The long run effect is to allow of a general development of capitalist production. The market is widened, and therefore production can be put on to an enlarged basis. This in turn is inevitably associated with a fall of  $\bar{x}$  and consequently with a fall in the rate of profit. Hence foreign trade, also, acts in a contrary sense on the two determinants of the rate of profit. First it raises the rate of surplus value: then it depresses the relative quantity of the variable capital.

Marx then considers briefly the question of whether the higher rate of profit earned by foreign investments should be reckoned into the general average rate of profit. He comes to the conclusion that, contrary to Ricardo, there is no reason

why it should not be. In the case of the British capitalist economy during the last fifty years, and to a lesser extent in the case of the other industrial empires, this consideration has evidently become of the very first importance. The rate of profit would long ago have sunk to an impossibly low level in Britain if the British empire had not offered unparalleled and semi-exclusive opportunities of foreign investment.

Here, then, we have the principal influences which check the tendency of the rate of profit to fall. It will be seen that they are closely bound up with the very force which is the father of that fall: Technical progress, in particular, and the development of capitalism, in general, check, by raising the rate of surplus value and by lowering the value of the physical mass of constant capital, that fall in the rate of profit of which they are the very cause. It is evident, also, that these influences can only check, not overcome, the main dominant tendency. The fall in  $\bar{x}$  which results from the growing productivity of labour must outweigh, in the long run, the increase in the rate of surplus value. The growth of the physical volume of constant capital must always cause an increase, though not a proportionate increase, in its value. Still the considerations of this chapter have enabled us to understand how it is that the capitalist system has not long ago become unworkable because of the fall in the rate of profit.

#### SUMMARY OF CHAPTER XVII

We have exhibited the basic difficulty in which the capitalist system finds itself. It cannot achieve its minimum rate of accumulation without so denuding the population of purchasing power as to cause a glut. And the rapidity of accumulation necessary to the system is determined by the speed of the fall of the rate of profit. It seems, then, that the system might well adjust itself to a moderate fall of the rate of profit. How fast, then, is that fall? If we judge by the contemporary facts of rationalization and mechanization in the world, that fall must be very rapid. Indeed, if this process, which we have called the fall of  $\bar{x}$ , is the only determinant of the rate of profit, that rate

must be in such precipitous decline that it is difficult to see how capitalism has survived at all. Yet it has, although with great difficulty, survived. Have we not proved too much? Even fifty years ago Marx felt this difficulty. But there are factors which counteract the fall of the rate of profit. They are: (a) the tendency of the rate of surplus value to rise. The rate of surplus value is the other determinant of the rate of profit. And this determinant is acted upon by the development of capitalist production in the opposite sense. There are limits, however, to the possibilities of offsetting the sag in the rate of profit by raising the rate of surplus value. (b) The growth of the physical volume of the constant capital is more rapid than the growth of the value of the constant capital. Thus  $c$  in  $\frac{s}{c+v}$  does not grow so fast as you would expect it to from the amount of rationalization which is going on. (c) Some forms of technical change raise the rate of surplus value, while depressing  $\frac{s}{c+v}$  less than usual. (d) The question of raising the rate of surplus value by depressing wages below their value. Marx's refusal to discuss this issue throws light on the whole *quæsitum* of *Capital*. (e) The possibility of raising the rate of surplus value by obtaining cheap imported necessities of life by means of foreign trade. The long run effect of foreign trade seen, however, to be the development of capitalist production and so a depression of the rate of profit. (f) The possibility of sustaining the average rate of profit by obtaining an exceptionally high rate on that capital which is exported. Importance of this device in Britain to-day. We see that all these counteracting tendencies are closely bound up with the very factor, the development of production, which depresses the rate of profit. We see, also, that they can check, but not overcome, the main downward tendency of the rate of profit.

## CHAPTER XVIII

### *Inevitability of Crises : How Recovery Comes : The Meaning of Over-Production*

THE last chapter has but served to emphasize the question which we raised in its opening paragraphs.

It is clear that the labour theory of value and the categories based upon it enabled Marx to exhibit the conditions necessary to the existence of the capitalist system. His analysis enables us to understand far better than any other the problems and tasks which face the capitalists. Having mastered it, we are no longer unable to comprehend why the seemingly obvious remedy for a crisis of glut, namely "a policy of high wages" and increased social services, is impossible of application. We can understand why the capitalist remedy for glut is, on the contrary, doubly to reduce purchasing power, by cutting wages and raising prices. Moreover, we are able to understand the desperate hunger for expansion, for markets, for opportunities of export and for foreign investment, which is causing every anxious empire to double and then redouble its army, navy, and air force.

But has Marx in showing all this done more than establish scientifically the conclusions to which the best capitalist theorists have, half instinctively, felt their way? Has he done more than give the *rationale* of the policies which capitalist leaders always pursue, guided by a century and a half of experience?

Moreover, now that we understand that the fall in the rate of profit is not so precipitous, at any rate, as it would be if it depended uniquely upon the magnitude of  $\bar{y}$ , now that we have allowed for the counteracting factors, is it not quite possible for the conditions necessary for the continued survival of capitalism to be fulfilled? We have pointed out a certain undeniable correspondence between the reasoning of the best capitalist theorists and the conclusions of Marx as to what these conditions are. But this is not to say that there is the slightest further agreement between them. The capitalist economists agree that accumulation must at all costs be maximized: that to this end wages must be kept down and social services curtailed even

though this must mean the end of any possibility of expanding the home market ; and that the " barriers " which stand in the way of the outward expansion of the leading industrial empires must be swept away. But they do not admit for a moment that it will ever be impossible to fulfil these pre-requisites of capitalism. They believe that it is perfectly possible for accumulation to be maintained in perpetuity at a sufficient rate to offset the falling rate of profit. They believe that the remaining undeveloped areas of the world offer substantial opportunities for renewing the youth of the system. They believe that, given the adoption of their specifics, capitalism can accumulate to infinity, for ever avoiding the occurrence of crises so catastrophic as to destroy it.

Nor is it a sufficient answer to this argument to point to the observed facts of continuing, ever recurring, and ever more catastrophic crises. The capitalist professors can retort that these symptoms are due merely to the mistakes of the leaders of capitalism. Under-consumptionist heresies, they may say, have undermined the capitalists' resistance to attempts on the part of the workers to raise their wages and social services to " uneconomic levels," and so have diminished accumulation : " protectionist fallacies " have checked the free expansion of the industrial empires into undeveloped areas and have caused those embittered inter-imperial rivalries which are, undeniably, leading the world to war. But all these things, they say, could have been avoided, and may possibly still be remedied, if only the voice of reason prevails.<sup>1</sup>

Marx's analysis, even so far as we have followed it, shows the extreme incredibility of any such stabilization of capitalism on the basis of ever accelerating accumulation, unhindered either at home or abroad. But we have not yet discussed the question of whether there is any extreme limiting factor which would inevitably produce crisis, even if all the conditions for maximum accumulation were fulfilled. In exhibiting this limiting factor it is necessary to emphasize that Marx conceived of it as a hypothetical case. He believed that before this limit was reached the basic dilemma, which we have defined above, would

<sup>1</sup> See the concluding paragraphs of Professor Robbins' *Nature and Significance of Economic Science*.



have precipitated crisis. He believed that it was impossible, in practice, to continue the process of accumulation at an ever accelerating pace without throwing on to the market an ever increasing supply of consumers' commodities. And, as we have seen, the very conditions, such as "an economic rate of wages," which made the process of accumulation possible, prevented the sale of this increased supply of consumers' commodities. It is, however, of the highest interest to follow the argument to its logical conclusion and exhibit what would happen if accumulation were successfully carried towards infinity.

The essential characteristic of a capitalist crisis, however precipitated, Marx says, is the simultaneous appearance of masses of unemployed capital and of masses of unemployed labour. This has indeed been the characteristic feature of every crisis, and above all of the great crisis which began in 1929. It is the simultaneous appearance of these apparently paradoxical phenomena which so troubles many capitalist economists. How *can* it be, they feel, that the masses of unemployed capital and the masses of unemployed labour do not come together? Surely, say the under-consumptionists, such as Mr. Hobson, Professor Fisher, or Mr. G. D. H. Cole, every kind of monetary expansion is legitimate, none is inflationary, until this has happened? Dr. Hayek and his school, it is true, advocate rather the cutting of wage rates and social services as a remedy for this situation. We have already seen, however, that monetary expansion and wage cutting are, in fact, but alternative ways of restoring the rate of profit. Hence implicit in the views of both capitalist schools is the idea that the masses of unemployed capital and labour do not come together because, if they did, the rate of profit which the unemployed capital would earn would be insufficient. Thus implicit (although in the case of the under-consumptionists, at any rate, they are totally unconscious of the fact) in the remedial proposals of all the capitalist economists is the view that for some unknown reason the employment of the additional capital held idle during a slump would drive the rate of profit down to an impossibly low level. Accordingly this new capital cannot be used, and the corresponding mass of workers cannot be employed, until and unless measures are taken to raise the existing rate of profit, and so offset the fall

in it which the bringing of the additional capital into use would cause. Thus there appears to be too much capital. There is a glut of capital. There is so much of it that it does not seem possible to employ it all at a tolerable rate of profit. Either some of it must stand idle, or measures, such as price raising and/or wage cutting, must be undertaken to raise the general rate of profit.

Now, asks Marx, will or will not these characteristic symptoms of crisis, which manifest themselves, from one aspect, as an over-production, or glut, or plethora, of capital, eventually appear even if accumulation has gone on unhindered in any way? Will an "absolute," unconditional over-production of capital occur inevitably? It will, even if accumulation is unhampered in any way, Marx writes, or rather it would, since he did not think that in practice this situation had ever arisen. The critical point will arise when further accumulation will *itself* cause the rate of profit to fall so steeply that the new augmented total capital will yield a lower amount of profit than did the old smaller total capital. The new augmented total capital will accumulate at such a much lower rate that its net yield of profit will be less than was the yield of the old smaller total capital at the higher rate of profit. Marx puts the point as follows:

"As soon as a point is reached where the increased capital produces no larger, or even smaller, quantities of surplus-value than it did before its increase, there would be an absolute over-production of capital. That is to say, the increased capital  $c + \Delta c$  would not produce any more profit, or even less profit, than capital  $c$  before its expansion by  $\Delta c$ ."<sup>1</sup> (*Capital*, Vol. III, chap. xv, p. 295.)

Moreover, he points out, accumulation will become unprofitable, and so will stop, and a crisis occur, even if the new augmented capital yields an amount of profit of the same, but of no higher, magnitude than did the old smaller capital. Let us take an illustration. Let us say that a capital of £2,000 yields £200 of profit, or 10 per cent. Let us say further that the same cause which increases this total capital to £3,000 reduces the

<sup>1</sup> The sign " $\Delta c$ " is simply Marx's shorthand for a new lump of capital, which is added to the old existing total capital  $c$ , so that we get " $c + \Delta c$ ."

rate of profit to 6·6 per cent. Then, in the new conditions, £3,000 will yield £198 of profit, or almost the same amount as before. But what sane capitalist will in such conditions perform the act of accumulation which increases his total capital from £2,000 to £3,000? Why, his only reward for saving the extra £1,000 and then for laying it out as capital, and so exposing it to all the risks of the market, is to reduce his profit by £2! "No, thank you," he will say, and will let his last £1,000 of accumulated profit, his last increment of capital, lie idle in the bank, even though he gets no interest at all on it, and will go on producing on the old scale with a total capital of only £2,000. *And it is, from one aspect, this action upon his part, and upon the part of his colleagues, which constitutes a crisis.*<sup>1</sup>

These conclusions are simple and arithmetical. But we have yet to allege that there is anything about unchecked accumulation, which does, in fact, suddenly plunge the rate of profit over a precipice so steep as to render the very next step of accumulation unprofitable. It can be shown, however, that unchecked accumulation would eventually have just this effect. For it would precipitate a new and sudden fall in the rate of profit by getting ahead of the growth of the population, raising the demand for labour, raising wages, and so lowering the determinant of the rate of profit, the rate of surplus value. If, Marx says, accumulation was so successful that it managed to keep well ahead of the fall of  $\bar{y}$ , it would begin, unless the working population was increasing rapidly too, to absorb the reserve army of unemployed, and so destroy one of the necessary conditions of capitalism. For this would stiffen wage rates and so

<sup>1</sup> The question naturally arises of how each individual capitalist knows that his and his colleagues' next act of accumulation will fail to yield an increased increment of profit for the capitalist class as a whole. The answer is that he doesn't. Hence in the ultimate stages of a boom that final and unprofitable act of accumulation is always performed. It is only after they have performed it that the capitalists discover that it has profited them nothing, since it has added nothing to the annual increment of profit. The capitalists as a class act in this matter blindly and unconsciously and therefore can only correct their policy as a result of trial and error. And this necessity for the capitalist class actually to experience the unprofitability of further accumulation in existing circumstances is, from one aspect, the explanation of the oscillations of boom and slump. It is because the capitalists always blindly carry their accumulation beyond the point at which it would have been, it subsequently turns out, profitable for them to have stopped, that the system is struck by sudden crises. At the same time all this expresses itself to the individual capitalist as so sharp a fall in the rate of profit that further accumulation is simply not worth his while.

begin to act upon the rate of profit by acting upon its other determinant, the rate of surplus value.

“There would be a strong and sudden fall in the average rate of profit, but it would be due to a change in the composition of capital which would not be caused by the development of the productive forces, but by a rise in the money-value of the variable capital (on account of the increased wages) and the corresponding reduction in the proportion of surplus-labour to necessary labour.” (*Capital*, Vol. III, chap xv, p. 295.)

We begin to see that Marx regarded any tendency for wages to rise as the most fatal thing which could possibly happen to the system. Though higher wages would do something to relieve the glut, they had a deadly effect on the rate of profit. Marx, we have said, did not regard this development as typical. He believed that, on the contrary, the reserve army of unemployed was destined to grow greater and greater. History has, in general, all too evidently confirmed his view. But even in the nineteenth century there were, as Marx clearly recognized, short periods of such rapid accumulation that the demand for labour power rose sharply (in spite of the fall of  $\frac{v}{c}$ ) and real wages tended to rise. And it seems probable that these boom periods were terminated (as they invariably were) by crisis and collapse just because this rise in wages checked the natural rise in the rate of surplus value, and so prevented this determinant of the rate of profit from offsetting the fall of  $\frac{v}{c}$ . Marx, as we shall see, called these periods of rising real wages “harbingers” of a coming crisis. We shall suggest below, moreover, that in the case of the situation of American capitalism in 1929, it may well have been something approximating to this hypothetical limiting factor which precipitated the crisis.

Indeed, it is clear that, from one point of view, a crisis precipitated by a labour shortage, a consequent bidding up of the price of labour power, and a consequent reduction in the rate of surplus value, causing a collapse of the rate of profit, already tottering from the fall of  $\frac{v}{c}$ , is to-day a more likely occurrence than it was fifty years ago. For to-day the population has

virtually ceased to grow in all the great industrial empires. Hence accumulation successful enough to offset the fall of  $\bar{v}$ , accumulation sufficient, that is to say, to increase the absolute magnitude of  $v$ , would at once begin to increase the demand for labour with a constant supply of labour. For we are rapidly approaching the point where there is no net annual increment of labour offering itself for exploitation. Hence it will soon be physically impossible to increase the magnitude of  $v$ , in the healthy way of increasing the number of workers employed at a given rate of surplus value; it will only be possible to increase  $v$  in the disastrous way of increasing the amount of capital which has to be used to employ a given number of labourers at a lower rate of surplus value. This leads us to the conclusion that the impending stabilization of the population, far from offering, as is often supposed, a solution for the problems of capitalism, will most seriously increase the difficulties of the system.<sup>1</sup>

This, then, is the ultimate limiting factor upon the possibilities of capitalist development. Nothing which capitalism can do can enable it to survive unless it can tap ever new supplies of exploitable labour. Even if prodigies of accumulation were accomplished, and thus the amount of profit realized were continually augmented, in spite of the ever falling rate of profit; even if this fall was itself minimized by the most rapid development of an imperial domain, a point would ultimately be reached when the next step of accumulation would result in the total capital of the community yielding a smaller, instead of a larger, amount of profit. Accordingly that next step of accumulation would not, and could not, be taken. The latest increment of profit would instead be kept idle. The characteristic symptoms of crisis, an unemployed mass of capital and an unemployed mass of labour, co-existing at the same time and place, would appear.

Our next task is to follow up Marx's analysis of what happens when the rate of profit falls below the point at which further accumulation pays ("pays" in the precise sense of yielding a

<sup>1</sup> As, however, we are dealing with the working population, not the total population, this situation of an absolute stabilization of the working population will be postponed for some time yet in Britain, and, I should guess, for longer still in America, since, owing to the rapid increase of the average age of the population, the number of persons of working age will continue to grow for some time after the total population has ceased to grow, or has begun to decline.

net increase in the amount of profit.) Nor does the way in which this crisis is precipitated affect its immediate consequences. The crisis may have been provoked, as Marx considered crises had in practice always been provoked, by an inability to dispose of an augmented supply of consumers' goods. Or it may have been provoked by the very speed of accumulation having bid up the price of labour power. In either case the next step of accumulation would have become unprofitable and so impossible. This is, in effect, Marx's account of the crisis phase of the trade cycle. Marx shows that the "solution" of keeping the new increments of capital as sterile hoards in the banks, which, we saw, must be the result of the outbreak of such a crisis, is not accomplished smoothly or easily. What has happened is that so much capital has now been accumulated that it cannot all earn an adequate rate of profit, that it cannot all earn, to be precise, that minimum rate of profit which will result in a greater total amount of profit than would the employment of a smaller amount of capital at a higher rate of profit. Thus some of the total capital, either the newly accumulated lump of capital (last year's profits) or some of the old and previously employed capital, must be held idle, for its use would depreciate the earning capacity of the total capital too much. But different portions of the total capital are owned by different capitalists. Hence the sore point arises of *whose* capital is to be held idle, and therefore earning no interest, in order to prevent the depreciation of everybody else's capital. This question can, naturally, only be settled by a process of jostling, by which each capitalist tries to grab for *his* capital the remaining opportunities of profitable investment.

Marx describes this jostling process as follows :

"It is evident that this actual depreciation of the old capital could not take place without a struggle, that the additional  $\Delta c$  could not assume the functions of capital without an effort. The rate of profit would not fall on account of competition due to the over-production of capital. The competitive struggle would rather begin because the fall of the rate of profit and the over-production of capital are caused by the same conditions. The capitalists who are actively

engaged with their old capitals would keep as much of the new additional capitals as would be in their hands in a fallow state, in order to prevent a depreciation of their original capital and a crowding of its space within the field of production. Or they would employ it for the purpose of loading, even at a momentary loss, the necessity of keeping additional capital fallow upon the shoulders of new intruders and other competitors in general.

That portion of  $\Delta c$  which would be in new hands would seek to make room for itself at the expense of the old capital, and would accomplish this in part by forcing a portion of the old capital into a fallow state. The old capital would have to give up its place to the new and retire to the place of the completely or partially unemployed additional capital.

Under all circumstances, a portion of the old capital would be compelled to lie fallow, to give up its capacity of capital and stop acting and producing value as such. The competitive struggle would decide what part would have to go into this fallow state." (*Capital*, Vol. III, chap. xv, pp. 296-7.)

These "jostlings," in the international field, are nothing less than those manœuvres for war positions which we are experiencing at the present moment. Thus we can describe the present struggle in Europe by saying that it is a struggle on the part of the British, French, Italian, and Czech capitalists to "load the necessity of keeping fallow the additional capital" upon the shoulders of the German capitalists, and of the struggle of these German capitalists to escape from the intolerable burden of carrying on their shoulders the immense weight of the idle capital of the Ruhr industries.

Marx now turns to the question of how a crisis can be overcome and recovery brought about. How can the struggle between the different capitalists as to whose capital is to continue to earn and whose is to be pushed into a profitless retirement be settled?

"How would this conflict be settled and the 'healthy' movement of capitalist production be resumed under normal conditions? The mode of settlement is already indicated by Sc

the mere statement of the conflict whose settlement is under discussion. It implies the necessity of making unproductive, or even partially destroying, some capital, amounting either to the complete value of the additional capital  $\Delta c$ , or to a part of it." (*Capital*, Vol. III, chap. xv, p. 297.)

How is this sterilization, or in the last resort actual destruction, of capital accomplished?

In the first place the diminution of production will itself lead to the physical deterioration of a part of the fixed and circulating capital. Factories and plants will rust and become obsolescent, stocks of perishable commodities will spoil or depreciate. There will be an actual, physical reduction in the mass of capital. But, above all, the process of the elimination of the redundant capital (redundant in the sense that its presence drives the rate of profit below the aforesaid critical point) is accomplished by a wholesale writing down of capital values. A catastrophic reduction of the value of everybody's capital is accomplished in different ways. In the first place, Marx points out, the value of what we should call "ordinary shares," or "equities," drops precipitously, as it is seen that the earning capacity of the productive system has decreased. For such shares are in essence but "creditors' notes" on future production.

The classical example of such a fall in equities or "creditors' notes" is the autumn of 1929 in New York. On October 23rd the Dow-Jones Index of the price of American industrial shares fell 21 points; in the next six days it fell 76 points more. By 1932 the United States Index of security prices, which had stood at 200-210 in 1929, had fallen to 30-40. This is incomparably the greatest and swiftest reduction in the value of a vast mass of constant capital in the history of capitalism.

From the point of view of those who own such securities the reduction of their value to a little over a tenth of what it was is the most catastrophic symptom of the crisis. We, however, are now in a position to see that this slaughtering of capital values is also a pre-requisite for the revival of the rate of profit, and so of the revival of production. For it is clear that the magnitude of  $\bar{y}$  will have been greatly increased. A large proportion of those redundant capitals, whose "jostlings" we described



just now, will have been eliminated. For the revival itself, however, further conditions must be fulfilled. Here is Marx's account of what would now be called "the upswing" of the trade cycle.

"At the same time still other agencies would have been at work. The stagnation of production would have laid off a part of the labouring class and thereby placed the employed part in a condition in which they would have to submit to a reduction of wages even below the average. . . . On the other hand, the fall in prices and the competitive struggle would have given to every capitalist an impulse to raise the individual value of his total product above its average value by means of new machines, new and improved working methods. . . . The depreciation of the elements of constant capital itself would be another factor tending to raise the rate of profit. The mass of the employed constant capital, compared to the variable, would have increased, but the value of this mass might have fallen. The present stagnation of production would have prepared an expansion of production later on, within capitalistic limits.

"And in this way the cycle would be run once more. One portion of the capital which had been depreciated by the stagnation of its function would recover its old value. For the rest, the same vicious circle would be described once more under expanded conditions of production, in an expanded market, and with increased productive forces." (*Capital*, Vol. III, chap. xv, pp. 298-9.)

It is evident that Marx believed that the essential agencies for restoring the rate of profit and so creating a revival were (a) reductions in wages, and (b) depreciation of the value of the constant capital. It is evident, also, that he believed that it *was* possible for the capitalists to solve particular crises if they could apply these remedies, and also the "external" remedy of the export of capital to undeveloped areas, thus relieving the congestion at home.

To sum up, a crisis manifests itself (a) in a glut of capital, or, as Marx calls it, "an over-production of the means of production"; (b) in mass unemployment, and (c) in the stagnation of

production. A crisis is overcome, in essence, by the effect on wages and on capital values of these very things. The glut of capital actually destroys some capital, and slaughters the values of all the rest of it. The glut of available labour drives down wages. The stagnation of production allows of the gradual sale of the "over-produced" commodities. Thus in time, and at the cost of colossal waste both of capital and of human beings, the rate of profit is restored. Hence a recovery becomes possible. It is once more possible to employ all the capital of all the capitalists at an adequate rate of profit. For the rate of surplus value has been screwed up by the fall in wages and at the same time there is now less constant capital left to employ. This completes Marx's description of the phases of the cycle of capitalist production.

It will be seen that Marx's analysis of crisis and recovery depends primarily on his conception of "over-production." (He speaks chiefly of the "over-production" of capital, but also of the "over-production" of commodities.) Hence it is essential to define precisely what he meant by an over-production either of capital or of commodities.

Of course, Marx points out, there can be no such thing as a general over-production of either commodities or capital *from an absolute social standpoint*. Mankind is still far from having achieved a sufficiency, let alone a surplus, either of goods or of means for the production of goods.

"It is not a fact that too many necessities of life are produced in proportion to the existing population. The reverse is true. Not enough is produced to satisfy the wants of the great mass decently and humanely.

"It is not a fact that too many means of production are produced to employ the able-bodied portion of the population. The reverse is the case." (*Capital*, Vol. III, chap. xv, p. 302.)

But, Marx continues, "it will not do to represent capitalist production as something which it is not, that is to say, as a production having for its immediate purpose the consumption of goods or the production of means of enjoyment for the

capitalists. This would be overlooking the specific character of capitalist production, which reveals itself in its innermost essence." (*Capital*, Vol. III, chap. xv, p. 303.) For capitalist production is "in its innermost essence" production for profit. And it is quite possible to understand how there can be an over-production both of capital and of commodities *for the purpose of making profit*. There most certainly can be "too many means of production and necessities of life to permit of their serving as means for the exploitation of the labourers at a certain rate of profit." (*Capital*, Vol. III, chap. xv, p. 303.)

The capitalist economists may prove, Marx writes with irony, that general over-production is inconceivable. But over-production is the predominating fact of the real world. The explanation is that general over-production for need or use *is* inconceivable. But this is a totally irrelevant consideration. For to-day production is undertaken, not for need, but for profit. And it is quite easy to understand how there can be over-production for the purpose of making profit.

"Otherwise, how could there be a lack of demand for the very commodities which the mass of the people want, and how would it be possible that this demand must be sought in foreign countries, in foreign markets, in order that the labourers at home might receive in payment the average amount of necessities of life?"<sup>1</sup> (*Capital*, Vol. III, chap. xv, pp. 301-2.)

"Capitalism," Marx writes, "comes to a standstill at a point determined by the production and realization of profit, not by the satisfaction of social needs."

A contemporary capitalist economist, Mrs. Barbara Wootton, has recently given us a striking example of the consequences of

<sup>1</sup> "This is possible," Marx continues, "only because in this specific capitalist interrelation the surplus-product assumes a form in which its owner cannot offer it for consumption unless it first re-converts itself into capital for him. Finally, if it is said that the capitalists would only have to exchange and consume those commodities among themselves, then the nature of the capitalist mode of production is forgotten; it is forgotten that the question is merely one of expanding the value of the capital, not of consuming it. In short, all these objections to the obvious phenomena of over-production (phenomena which do not pay any attention to these objections) amount to this, that the barriers of capitalist production are not absolute barriers of production itself." (*Capital*, Vol. III, chap. xv, pp. 301-2.)

a failure to appreciate the importance of the essentially profit-making character of capitalist production. In an early passage in her book, *Plan or No Plan?* she amply recognizes the prior necessity of the emergence of profit, not only, as she neatly shows, as an incentive, but also as a regulator of the capitalist system. She writes :

“Movements of profit take precedence of all other price changes, since the prospect of profit is ordinarily the *first* indispensable stimulus to production. It is only after someone has smelled a profit in the air, that the workers, whose job it is to make the goods that meet the demand that offers the profit, have a chance to get to work. In other words, the satisfaction of consumers' needs is achieved, so far as it is achieved, first through the stimulus of profit, and only secondarily and indirectly because a hungry and eager consumer is a magnet for workers equally eager to make him what he wants. So also the consumer goes without, when the utmost price that he can and will pay is insufficient, not just to provide a living for those who would work for his satisfaction, but rather to yield a profit that will induce someone to employ those would-be workers.” (*Plan or No Plan?* chap. i, p. 44.)

One would have thought that this was clear enough. What must be our surprise, then, to find that by page 247 Mrs. Wootton has forgotten all about the necessity of the appearance of profit if production is to be undertaken. She suddenly regresses to the view that the object for which capitalism works is the production of useful goods. In discussing the prospects of the American New Deal she writes :

“To me, at least, it is difficult to believe that the vigorous and gifted inhabitants of that country will not again make at least as good a success as they have done in the past of the fundamentally simple business of exchanging the products of their various activities to their mutual advantage.” (*Plan or No Plan?* chap. v, p. 247.)

But the object of American capitalism is not the fundamentally simple business of swapping use values to the mutual advantage

of the swoppers. The object of American, as of every other, capitalism is to distil new value, in the form of profit, out of the process of production and to add this new value to the existing pile of accumulated capital. And the wheels of production, as Mrs. Wootton has previously so clearly recognized, will only turn *if their turning does result in this distillation.*

A failure to distinguish the nature of profit lies behind Mrs. Wootton's phrase "to their mutual advantage." Naturally different producers and groups of producers can exchange diverse use values "to their mutual advantage" in the sense that the appropriate use values can be united to the appropriate consumer. This is what happens in socialist exchange in the U.S.S.R. And this process, as she says, is "a fundamentally simple business"—though it may be by no means a simple business to devise the best methods of carrying it on. But no "mutual advantage," in the sense of new value, in the sense of profit, can possibly arise, as Marx demonstrated at the beginning of *Capital*, to the capitalists of a country from exchanging their products. Profit can only arise during the process of production itself. And the re-creation of the conditions under which profit (in sufficient volume)<sup>1</sup> can again be extracted from the process of production is, in present day America, anything but "a simple business." Yet American capitalism can never flourish again until and unless this can be accomplished.

Now if capitalism were a system of the character which Mrs. Wootton sometimes supposes it to be, directly producing use values for their own sake, then, indeed, it would be impossible to understand how there could be a general over-production of either commodities or capital. We have already seen, however, that if your object is to achieve the maximum net annual increment of profit, then, in certain conditions, it will be better not to use all your existing capital. And these conditions are that the use of all your capital will drive the rate of its increment, the rate of its self-expansion, below the point at which the larger capital will yield a larger increment of profit than the smaller capital. When this situation arises, and we have seen that it does arise in practice, and must arise in theory, there will be

<sup>1</sup>To be precise, in sufficient volume to give the necessary minimum rate of profit on the vast mass of America's accumulated capital.

quite definitely too much capital in existence for the purpose of producing profit, or new capital. There will be undeniably, and perfectly rationally, an over-production of capital *for this purpose*.

In these circumstances an enlargement of the scale of production cannot be undertaken. For the maximization of the amount of profit, the self-expansion of capital at the maximum rate, is the be-all and end-all of the system. It is foolish and useless to gird at the system for obeying this law : for ceasing to produce just so soon as further production would decrease, and not increase, the net amount of profit obtained. We may point out that men and women are dying for the want of an increase of production and that there is no physical obstacle whatever to their desperate needs being satisfied. But capitalism, to do it justice, never pretended to be a system for the direct satisfaction of human needs. On the contrary, capitalism's claim was that if men were allowed to seek, not to satisfy human needs, not to serve society, but to maximize their own profits, then, indirectly, but none the less surely, human needs would be satisfied and society served. Use values, means of enjoyment and consumption, that is to say, were, under this implicit social contract between mankind and capitalism, to emerge, not as the direct objective of production, but as a kind of by-product.

Production was to be undertaken in order to obtain the maximum profit ; and it was to be undertaken only if and when it would serve this purpose. But faithful adherence to this purpose would in fact, it was claimed, give the world an incomparable supply of use values, or consumable commodities. For the laws of society and the laws of nature were said to be of such a kind that profit could only be produced if consumable commodities were supplied. The supply of consumable commodities would be, it is true, only a by-product of the process of the production of profit. But it would be an inevitable by-product, and society could be assured of this supply being forthcoming. Indeed, the great advantage claimed for this arrangement was that thus, and only thus, could men's primitive and powerful instincts of self-aggrandizement be harnessed to the car of universal plenty. The capitalists, it was declared, would seem to themselves to be working for their own profit ; but, as they

could only obtain their profit by supplying us all with commodities, they would in fact be working for us.

This was the implicit contract (if the reader will permit a mythological image) which society made with capitalism. It is useless, then, to express horrified surprise when the capitalists regulate their production with a view to the maximization of profit and nothing else. It is ignorant to say that over-production is impossible while millions of men and women are destitute. An over-production of commodities takes place when the particular individual commodity is produced which by its appearance on the market so depresses the price offered for the whole supply that the augmented supply sells for a lower total amount, or even no higher an amount, than the old smaller supply would have sold for if that last fatal commodity had not appeared. The over-production of capital takes place the moment the last critical pound of capital so depresses the rate of profit that the new augmented mass of capital yields a lower, or no higher, increment than did the old, smaller, mass of capital. When that point comes neither the piety of the philanthropists, who depict the world's miserable ocean of unsatisfied needs, nor the wit of the critics who spend their irony on pointing the starvation in the midst of plenty paradox, can make the system produce another bushel of wheat or another ton of coal. Perfectly and necessarily obedient to the pull of profit, capitalism decreases production when it pays it to do so, just as inevitably as it increases production in the opposite circumstances.

Some of the most important passages in the third volume of *Capital* elucidate this conclusion and expatiate upon it. In particular, we are now in a position fully to understand the inevitability under capitalism of the co-existence of quantities of unemployed labour and capital. Marx writes :

“ It is no contradiction that this over-production of capital is accompanied by a more or less considerable relative over-population. The same circumstances, which have increased the productive power of labour, augmented the mass of produced commodities, expanded the markets, accelerated the accumulation of capital both as concerns its mass and its value, and lowered the rate of profit, these same circumstances have also

created a relative over-population, and continue to create it all the time, an over-population of labourers who are not employed by the surplus-capital on account of the low degree of exploitation at which they might be employed, or at least on account of the low rate of profit which they would yield with the given rate of exploitation." (*Capital*, Vol. III, chap. xv, p. 300.)

*This is the simple and sufficient reason why there is nothing absurd or even paradoxical, for the purposes of capitalism, for the purpose, that is to say, of the production of the highest possible amount of profit, in the co-existence of unemployed workers and unemployed capital.* To bring them together would so reduce the rate of profit as to decrease, instead of increase, the net amount of profit being made. Accordingly, they can only be brought together if wages are reduced, or prices raised, sufficiently to push up the rate of surplus value to a point which will make production on a larger scale compatible with a net increase in the amount of profit. This is the answer to all those capitalist thinkers, from Mr. Keynes to the simplest Rotarian, who, as we have seen, believe that general over-production, and a consequent co-existence of unemployed labour and capital, is an absurd paradox which proves that all that is wrong with capitalism is some "flaw" in the banking system. The co-existence of these two things *would be* absurd if the objective of the system was the production of the maximum amount of consumers' commodities. But the objective of the system is the production of the maximum amount of profit, not of the maximum amount of consumers' commodities. *And for this purpose* it is easy enough to have too much capital and too many commodities.

Finally it is the appearance of this extraordinary phenomenon, over-production, which shows us that capitalism must, and will, outlive its function. For the appearance of over-production demonstrates that the rate of profit is no longer adequate to sustain a further development of the productive forces. When over-production becomes chronic, it means that the rate of profit can no longer be restored, even temporarily, to a level high enough to permit of the employment of all the available capital and labour. Capitalism's function was to industrialize the



world : to build up, under the spur of profit, those indispensable means of production which can alone enable men to live securely and plentifully. While that task was in the doing production was profitable. By and large, and with only intermittent crises, it was possible to maintain such an acceleration of the rate of accumulation that, in spite of everything, the amount of profit and employment was increased. There was some sort of rough correspondence, at any rate, between profitability and social need. To-day this is less and less true. The basic foundations for the production of wealth have been laid. The criteria of profitability and social need diverge ever more widely. Marx concludes this phase of his argument with a sweeping passage.

“ The rate of profit is the compelling power of capitalist production, and only such things are produced as yield a profit. Hence the fright of the English economists over the decline of the rate of profit. That the bare possibility of such a thing should worry Ricardo, shows his profound understanding of the conditions of capitalist production. The reproach moved against him, that he has an eye only to the development of the productive forces regardless of ‘ human beings,’ regardless of the sacrifices in human beings and capital *values* incurred, strikes precisely his strong point. The development of the productive forces of social labour is the historical task and privilege of capital. It is precisely in this way that it unconsciously creates the material requirements of a higher mode of production. What worries Ricardo is the fact that the rate of profit, the stimulating principle of capitalist production, the fundamental premise and driving force of accumulation, should be endangered by the development of production itself. And the quantitative proportion means everything here. There is indeed something deeper than this hidden at this point, which he vaguely feels. It is here demonstrated in a purely economic way, that is from a bourgeois point of view, within the confines of capitalist understanding, from the standpoint of capitalist production itself, that it has a barrier, that it is relative, that it is not an absolute, but only a historical, mode of production corresponding to a definite and

limited epoch in the development of the material conditions of production." (*Capital*, Vol. III, chap xv, pp. 304-5.)

In this passage Marx, standing at the very centre of the capitalist period, casts his eye forward and back over the whole life history of the system. To-day it is plain that the definite and limited epoch in which capitalism could perform its task and exercise its privilege has closed. The productive force of social labour has been developed to the utmost extent to which it can be developed by capitalism. Othello's occupation's gone.

#### SUMMARY OF CHAPTER XVIII

Marx has shown the conditions necessary to the existence of capitalism. But cannot these conditions be fulfilled, as the capitalist economists maintain? Why should crises be inevitable? Crises will occur even if accumulation is maximized. The characteristic symptom of crisis is the co-existence of unemployed labour and capital. This paradoxical symptom baffles the capitalist economists. Yet all their remedies for it turn out to be to raise the rate of profit. This gives us a hint of why this glut of unemployed capital has appeared. It has appeared because the next step of accumulation would decrease, instead of increase, the amount of profit. Why? Because the next step of accumulation would bid up the price of labour power, and so shatter the rate of profit by acting on its other determinant, the rate of surplus value. This is the ultimate limiting factor of capitalist development.

What happens when the next step of accumulation becomes impossible, because unprofitable? This is the crisis. For the solution of keeping some of the capital idle and useless in the banks cannot happen easily or smoothly. For *whose* capital is to be kept idle? The resultant jostlings described.

How recovery comes. Marx's account of the upswing of the trade cycle. It is accomplished (*a*) by the elimination of the redundant capital, both by the physical destruction of some of it

and by the shrinkage in the value of all of it ; and (b) by the reductions in wages made possible by the growth of unemployment and by the encouragement of rationalization. Thus the familiar and painful symptoms of crisis are themselves the remedial agencies.

It will be seen that Marx's theory of both the crisis and the recovery depends upon his concept of over-production. Hence it is necessary to elucidate exactly what he means by an over-production of capital and of commodities. Naturally there can be no question of an absolute over-production of either. Men have not enough of either capital or commodities *for their use*. But, Marx declares, it will not do to regard capitalism as having the production of useful commodities as its immediate purpose. For the immediate purpose of capitalist production is profit. And *for this purpose* there certainly can be a general over-production of both capital and commodities.

The necessity of this warning is illustrated by Mrs. Wootton's hesitations on the subject. In one passage she emphasizes, but in another ignores, the prior necessity of the distillation of profit if capitalist production is to be undertaken.

*If* capitalism were the kind of system Mrs. Wootton supposes it to be, then over-production would be incomprehensible. But we have already seen precisely how the production of too much capital and too many commodities for the purpose of making profit can, and does, occur. It is foolish to complain of capitalism obeying the laws of its own nature. The implicit social contract between mankind and capitalism. Neither our piety nor wit will make capitalism cancel half a line of that contract. We can now see fully why the capital and the labour unemployed in a slump cannot be brought together until the rate of profit has been raised. Recapitulation of the *impossibility* of general over-production for use, and of the *fact* of general over-production for profit. The nemesis of the falling rate of profit foreseen by Ricardo. "The fright of the English economists." Othello's occupation's gone.

## CHAPTER XIX

### *The Dilemma of Profit or Plenty Restated*

WE have now exhibited Marx's analysis of the economic cycle. We have shown how and why it becomes periodically impossible any longer to offset the falling rate of profit by an accumulation sufficiently rapid to increase the amount of profit. For either wages, etc., must be kept so low that it is impossible to sell the ever increasing supply of consumers' goods, or wages must be allowed to rise sufficiently to act upon the rate of surplus value and so precipitate the rate of profit over a precipice. We have shown why this must, and does, produce a falling off of production and the simultaneous appearance of masses of unemployed capital and labour. We have further shown how these crises can, in certain circumstances, be overcome and the rate of profit restored to a level which will again permit of the employment of all the factors of production.

We must now look more closely into the way in which this recovery (which is in essence a recovery in the rate of profit) is effected. It is effected, we have already seen, by two processes. In the first place the crisis itself physically destroys some of the accumulated constant capital. In Marx's day this was an automatic process. Some of the productive plants depreciated from disuse. Some of the stock of perishable commodities inevitably became unusable. To-day brisker and more deliberate measures are necessary. Cotton, coffee, wheat, hogs, oranges, fish, and many other commodities are carefully destroyed, in order that the price of the remainder may be raised to profitable levels. In the same way whole productive plants are scrapped in the most orderly and business-like manner imaginable. That *doyen* of capitalist institutions, the Bank of England, has, for example, organized a company for the special purpose of destroying British shipyards. It is called "National Shipbuilders Security Ltd.," and one of its objects, as laid down in its memorandum of association, is "to assist the shipbuilding industry by the purchase of redundant and/or obsolete shipyards, the dismantling and disposal of their contents, and the re-sale of the sites under restrictions against further use for shipbuilding." Nor has "National

Shipbuilders Security Ltd." allowed the grass to grow under its feet. In its determination to see to it that grass shall grow instead in some of the shipyards of Britain the Company had up to the end of 1933 closed down or destroyed 100 shipbuilding berths.<sup>1</sup> An analogous company has been formed in the British wool textile industry under the title of "The Woolcombers Mutual Association Ltd.," and action of an analogous character is now widespread throughout the entire capitalist system. (For a full account of these forms of well organized destruction, see R. P. Dutt, *Fascism and Social Revolution*, pp. 45-6.) (Incidentally, here is a real case of Marx's theories having become out of date. Marx had no conception of the organized destruction which latter-day capitalism would employ for the solution of its crises. His account shows that he was a child in such matters. Strange that his capitalist critics, who never tire of alleging that Marxism is hopelessly obsolete, do not seem to care to point out this deficiency!) In Marx's time, however, and even to-day (we instanced October 1929), the main work of reducing the constant capital is done, not by the physical destruction of part of this capital, but by a general (though not uniform) reduction of the value of the whole mass. This is one side of the restorative work of a crisis. The magnitude of  $c$  in  $\frac{c}{v}$  is reduced and the rate of profit correspondingly revived. It is this aspect of crises which makes Marx call them "momentary and forcible solutions of the existing contradictions, violent eruptions, which restore the disturbed equilibrium for a while."

But in all recent crises this partial restoration of the previous magnitude of  $\frac{c}{v}$  has been quite insufficient to restore by itself the rate of profit sufficiently to set the wheels of production turning again. It has been urgently necessary to act upon the other determinant of the rate of profit, the rate of surplus value.

<sup>1</sup> Including the entire shipyards, which were its sole means of life, of the town of Jarrow. Mr. Walton, the last employed clerk of the Jarrow shipyards, spoke as follows in an interview with Mr. Ian Coster published in the *Evening Standard*, October 9th, 1934 :

"Until to-day there were two of us. I paid the other man off to-day. That leaves me and the manager and a few watchmen. . . . Jarrow, you see, was a one-industry town. There were chemical works and paper mills but they went a good while ago.

"And now the Shipbuilders Security have got the yard there cannot be another ship built here for 40 years. The blast furnaces and the steel works are being torn down."

Now the rate of surplus value can only be raised in two ways. Either the rate of money wages must be reduced or prices must be raised.<sup>1</sup> In either case the effect is clear. The rate of profit will be raised, yes. *But only by reducing the amount of consumable goods which can be sold within the economy in question : by reducing the net consuming power of the population.*

Now Professor Robbins, as we have seen, says that a slump is due to the fact that "demand at the consumer's end has become relatively too high." (*The Great Depression*, p. 70.) No diagnosis of crises, a characteristic of which has invariably been an overwhelming glut of consumers' goods, could be more paradoxical. How can we say, for example, that the 1929 slump which was characterized by a gigantic glut of consumers' goods, was caused by demand at the consumers' end having become relatively too high? This, at least, is a preposterously obscure way of describing the situation. For clearly consumers' demand was *too low* to absorb the huge volume of consumers' commodities which was coming on to the market in 1929. We are now, however, in a position to see what Professor Robbins is getting at. While consumers' demand was unquestionably too low to absorb the output of consumers' goods (at profitable prices), it may be true that it was at the same time too high to allow of a rise in the rate of surplus value sufficient to offset the very rapid fall of  $\frac{v}{c}$  which was going on. It may be true that it was the rise in real wages, the very rise in consumers' demand, which undoubtedly took place (this is described in Chapter XX) in 1929 and 1930, which precipitated the slump. For this rise, while it was too small to do much to relieve the glut of consumers' commodities, may have been large enough to prove the last straw to the rate of profit.

Hence there is nothing peculiar, from the capitalist point of view, in it being necessary to reduce purchasing power at the consumers' end, thus restoring the rate of profit, in order to secure a revival. But there is, of course, something very peculiar indeed about this procedure as a means of establishing

<sup>1</sup> It is worth noticing that these are precisely the same thing under different names. For it is an increase in the price of necessary articles of working-class consumption, which alone increases the net intake of profit of the capitalist class as a whole. A mere increase in the price of producers' goods, or of luxuries consumed by the capitalist class, will, obviously, impoverish some capitalists as much as it enriches others.

permanent capitalist stability. For, if it is necessary to cut down the consumption of consumers' commodities to a minimum in order to secure a revival in productive activity, then this necessity leads straight towards a fresh interruption of that activity from an inability to sell the commodities which will come on to the market as a result of the revival of productivity. Marx points the paradox thus. Production at a profit is only half the battle for the capitalists.

"Production of surplus-value is but the first act of the capitalist process of production, it merely terminates the act of direct production. Capital has absorbed so much unpaid labour." (*Capital*, Vol. III, chap. xv, p. 286.)

Very good, but now this mass of profit which is embodied in a great mass of commodities of every kind must be sold. For the capitalists, unlike primitive landlords, do not want this mass of commodities for their own use. They must turn them back into money, and then use this money to buy the raw materials (including the labour power) which will become in the next cycle of production another immense mass of commodities, which again must be sold.

And the very measures (such as wage reductions or price increases) which enable the capitalists to win the first half of their battle, *viz.*, to produce at a profit, must ultimately prevent them from winning the second half of their battle: must tend to prevent them from selling their commodities. For "the consumption of the great mass of the population" has to be kept down, "to a variable minimum within more or less narrow limits." Thus we see again that *the very measures which make production profitable tend to make consumption impossible.*

This, we recollect, was the dilemma which we unearthed in Part I. We saw then that in one sense the under-consumptionists were not wrong. They were perfectly justified in saying that continual reductions in purchasing power were an insane method of attempting to distribute a glut of commodities. They overlooked, however, that this policy, whatever its effect on consumption might be, was the only way in which the capitalists could make production adequately profitable again, and was therefore the only way in which the wheels of capitalist industry

could be set turning. They saw one horn of the dilemma of profits or plenty, but not the other.

We are now in a position to realize that the repeated reductions of consumers' purchasing power, by which the capitalists attempt to overcome each crisis, inevitably prepare the next crisis. For such a policy re-creates the very conditions which produced the crisis. Or rather, it re-creates these conditions in an aggravated form.

"Capitalist production," Marx writes, "is continually engaged in the attempt to overcome these imminent barriers, but it overcomes them only by means which again place the same barriers in its way in a more formidable size." (Vol. III, p. 243.) The barriers not only reappear, but reappear on a more formidable scale. For the market has been narrowed. The base upon which the whole towering structure of production rests has been contracted.

This conclusion strongly reminds us of Dr. Hayek's argument. For this we recollect, was Dr. Hayek's own description of the situation. His solution for every crisis is to narrow, relatively, the base of his triangle representing the structure of production, by heightening the apex. In his language, production must become more "capitalistic," more "round-about." More resources must be used at the higher end of the structure, more men must be employed in making machines to make machines to make machines, so that the total production of consumable goods will remain constant and the entire increase in society's productive power be devoted to increasing still further society's productive power. The structure of production must get longer and longer. The sides of the Hayekian triangle must be produced and produced. This, then, is the Hayek-Robbins solution of the dilemma.<sup>1</sup> It is possible, they imply, for all the conditions which are necessary to the existence of capitalism to be fulfilled simultaneously. It is possible for wages to be kept down to "economic levels," and yet for there to be no glut of consumers' commodities. For if the demand for consumers' commodities is thus minimized, no excess of consumers' commodities will be produced. The entire increase of society's productive power

<sup>1</sup> As we noticed in Part I, the professors do not clearly draw this conclusion themselves. But it is the conclusion towards which their whole argument points.



will be devoted to increasing the production of producers' goods. And if this is done, then there will be no need to increase the ultimate market. The entire increase in the supply of commodities will be an increase in producers' commodities, which can be absorbed *within* the structure of production. For that structure will be getting longer and longer. Hence there will be no need for any increased supply of actual consumers' commodities ever to emerge from the productive process. Industry can take in its own washing on an ever more gigantic scale, and for ever. The overwhelming majority of mankind can continue to live on a subsistence level in perpetuity and our ever growing powers of production can be permanently absorbed by the task of producing new means of production. Thus there need be no crises. Capitalism need never feel the lack of a larger market for consumers' goods, for it will never increase the production of consumers' goods. *The market for which capitalism will produce will be within itself. It will be within its own ever lengthening structure of production.*

What are we to say of such a solution? There is no need to deny that it has a sort of insane logic. But our criticism of it cannot be confined to pointing out the dementia of increasing to infinity the production of means of production, while never actually increasing production itself.<sup>1</sup> We must point out also that in fact capitalism does not, and never has, worked in this way. In every period of expansion, such as that of the nineteen-twenties, the actual production of consumers' commodities, and far more the capacity to produce consumers' commodities, has grown as well as the production of means of production. One has only to think of the increase in American agricultural production, and above all in American agriculture's capacity to produce, to realize this. Or again the statisticians of the New Deal recently investigated the boot and shoe industry of America. They discovered that America has created three times

<sup>1</sup> This is in one sense an overstatement. For the production of consumers' commodities has to be, and has been, increased if and when the new technique of production requires types of workers (e.g., literate workers) who are more expensive to produce and maintain. In this case the subsistence level of wages itself rises. The value of labour power increases. This is the basic reason for the rise in the workers' standard of living which took place in the last century. But the technique of production is now changing again, so that fewer skilled and literate workers are needed. Accordingly the true subsistence level of wages is probably falling.

the amount of productive plant necessary to the production of as many boots and shoes as the American people could use, even if they all had enough money to buy all the boots and shoes they wanted !

These examples make clear how remote from reality is the Hayek-Robbins vision of the entire increase in society's productive capacity being absorbed in the upper reaches of the producers' goods department, so that it need never result in any increase in consumers' goods.<sup>1</sup> The truth is that part of the new investment is bound to slop over into increasing productive capacity in the consumers' goods department, and finally into actually producing an increased supply of consumers' goods. And it is usually this fatal necessity which precipitates the crisis. For there can have been distributed no adequately increased supply of money to the non-capitalist elements of the population ; thus glut, a sudden fall in prices, and all the familiar catastrophes of a crisis, must follow.

The Hayek-Robbins school would scarcely deny, we may suppose, that this is what actually happens. They would allege, however, that this is only because of the weakness and errors of the human agents who work the system. They would say that this growth in the production of consumers' goods, this misdirection of investment on to the lower reaches of the structure of production, was the consequence either of failing to cut money wages as prices fell, or of injecting new money into the system. They would say that an over-production of consumers' goods was, paradoxically, the other consequence of allowing the incomes of non-capitalists to exceed subsistence and so curtail accumulation. But by this time the argument has become highly abstract. *If* it was rational never to use our ever increasing productive capacity to provide us with any increase in consumers' goods ; *if* it was possible to confine all new investment to the upper reaches of the structure of production ; *if* it was possible to absorb the whole increase of the production of commodities within the structure of production, so that no increased supply ever emerged from that structure ; *if* it was possible so to compress demand at the consumers' end, and so

<sup>1</sup> As we saw, Mr. E. F. M. Durbin noticed this extraordinary implication in the Hayek argument and was much disturbed by it.

to expand it at the producers' end, that the sides of the Hayekian triangle were infinitely produced ; *if* it was not insane to propose to occupy the human race, kept for ever on subsistence rations, in perpetuity with the task of making machines to make machines to make machines ; then capitalism might be immune from crises. But does this conclusion provide us with a solution for the dilemma ? Is it not quite as much a *reductio ad absurdum* as a solution ?

For what has been demonstrated is, in fact, that the contradiction between an ever mounting power to produce and a power to consume, which for the mass of humanity must never grow above subsistence, must become more and more intolerable.<sup>1</sup> No one but a capitalist economist would dream that such a situation could produce anything but what it does produce, a series of crises, each of which is more severe than the preceding one. Each crisis is more severe because the task of squeezing the base of the structure of production and pulling out the apex, of devoting all new productive power to the producers' goods department, of maintaining accumulation at a sufficient rate to offset the fall of  $\gamma$  (for these are all different ways of saying the same thing) has become still more difficult than it was last time.

The "barriers" to capitalist production consist, then, in the last analysis, in the fact that capitalism is a system which works only for the production of profit ; which works, that is to say, for the production of increments of new capital to be added to the existing mass of capital, and that it can only produce commodities if and when their production will have this effect. But capitalism, because it is both nationally and internationally competitive, must also continually develop the productive power of society. For a period these means, *viz.*, the development

<sup>1</sup> We notice that increased luxury expenditure on the part of the rich (which is sometimes suggested as a capitalist cure-all) would make matters worse, not better. For it, too, involves the deflection of funds from the all-important task of accumulation. It is itself one of the elements of a relatively over-high demand at the consumers' end. And Professor Robbins actually attributes some importance in the precipitation of the 1929 crash to the spending, instead of accumulation, of their speculative profits by the American capitalists. But he fails to see that, while accumulation might no doubt have been accelerated by greater thrift, such action would have narrowed the market for consumers' goods still more and so have precipitated the crisis even earlier. As usual, the capitalist theorist can only see one or other of the horns of the dilemma, but never both.

of the community's powers of production, are consonant with this aim, *viz.*, the maximization of profit. But there must come a time (and to-day we must write there *has* come a time) *when the further development of society's productive powers ceases to maximize profits, and begins, on the contrary, to diminish them.* This can mean nothing but that capitalism has outlived its function. The cunning device by which the formidable force of private aggrandizement was harnessed to the social purpose of industrializing the world has broken down. The private interest of the capitalists in maximizing their profits no longer pulls in the same direction as the public interest of developing society's means of production. They begin to pull in opposite directions. It is at this point that capitalism becomes, and must become, "disloyal to its mission."

"Its historical mission is the ruthless development in geometrical progression, of the productivity of human labour. It becomes disloyal to its mission, whenever it puts a check upon the development of productivity, as it does here. Thus it demonstrates once again that it is becoming weak with age and more and more outliving its usefulness."<sup>1</sup> (*Capital*, Vol. III, chap. xv, p. 308.)

When this point has been reached we have entered the period of the general and permanent crisis of capitalism. This is the period in which we live to-day. The period of the general crisis of capitalism may be said to have begun in 1914 and to have persisted ever since. This fact is recognized, as we saw, by the best capitalist authorities. Professor Robbins wrote, "We live, not in the fourth, but in the nineteenth, year of the World Crisis." (*The Great Depression*, p. 1.) But this general crisis, which is the manifestation of the fact that capitalism has outlived its

<sup>1</sup> This passage is by Engels. It forms part of one of the interpolations which Engels made during his revision of the manuscripts of Vol. III of *Capital*. Incidentally a mass of nonsense has been written (and repeated by Mr. Raymond Postgate) to the effect that it is impossible to know what parts of Vols. II and III are "really" by Marx and what are "mere" excogitations by Engels, etc., etc. These critics have not, it seems, taken the trouble to read Engels' preface to Vol. III, in which he states in the most precise manner possible just exactly what parts of the MSS. he revised and the extent of his revisions. Moreover, they have apparently omitted to notice that wherever the text "passes," as Engels says, "in some points beyond the scope of the original material," Engels puts the whole passage within square brackets and affixes his initials "F. E."

function, does not come on gradually or smoothly like a creeping paralysis. On the contrary, the decline of the rate of profit acts on the system by a series of ever more severe jerks. These jerks are the cyclical crises which still persist as oscillations around a descending curve. For there are, as we have seen, practicable and important measures by which the decline of the rate of profit can be, and often has been, arrested, and even for a time reversed. But the nemesis of these measures is that they are all of such a kind that, although at first they check and reverse the falling tendency of the rate of profit, yet their secondary effect is to prepare the way for a new and even more precipitous fall.<sup>1</sup> For they make the realization of profit by the ultimate sale at profitable prices of all the commodities produced ever more impossible. Thus all the various contemporary policies for "recovery" cannot conceivably do more than stave off the bankruptcy of the system. They are more and more taking on the character of reckless and convulsive efforts which, while they bring relief, bring it for ever shorter periods and at an ever higher price. For they do nothing, and can do nothing, to alter the basic dilemma of capitalism.

Marx has several passages in which he sums up that dilemma. Perhaps the most striking is the well known paragraph on p. 293 of Vol. III. In a rational society, he explains, the production of consumable commodities, of use values, would be the object of economic activity; the development of the productive powers of society would be but a means to that end. But it is the peculiar nature of capitalism that what would be a rational society's end, is capitalism's means, while what would be a rational society's means are capitalism's end. Moreover, at a certain point capitalism's means cease to serve its end and are consequently abandoned. Yet these means, *i.e.*, the production of a supply of use values, are what matter for everybody except the capitalists. Under capitalism the workers are able to live only because the capitalists were (and, of course, to some extent still are) able to maximize their profits by paying the workers wages; by giving them, that is to say, a supply of use values.

<sup>1</sup> Hence the inevitable analogy of the drug addict. "The shot in the arm" analogy is often instinctively, but correctly, applied to policies of the type of the American New Deal.

The workers' sustenance is, as we phrased it, a by-product of a system of which the essential products are increments of capital. The moment, therefore, that the giving of wages or other means of existence to non-capitalists ceases to maximize the profits of the capitalists, wages must cease to be given. The means have come into conflict with the ends.

*"The real barrier of capitalist production is capital itself.* It is the fact that capital and its self-expansion appear as the starting and closing point, as the motive and aim of production; that production is merely production for *capital*, and not *vice versa* the means of production mere means for an ever expanding system of the life process for the benefit of the *society* of producers. The barriers, within which the preservation and self-expansion of the value of capital resting on the expropriation and pauperization of the great mass of producers can alone move, these barriers come continually in collision with the methods of production, which capital must employ for its purposes, and which steer straight toward an unrestricted extension of production, toward production for its own self, toward an unconditional development of the productive forces of society. The means, this unconditional development of the productive forces of society, comes continually into conflict with the limited end, the self-expansion of the existing capital." (*Capital*, Vol. III, chap. xv, p. 293.)

Palme Dutt begins his *Fascism and Social Revolution* with a startling example of the now insuperable barriers which stand in the way of capitalism when it attempts to utilize the latest developments of science and technique. He quotes the *Automobile Engineer* for March, 1931. This journal cites a paper delivered by Mr. H. C. Armitage to the British Institute of Automobile Engineers. Mr. Armitage demonstrated "that the high-production machines that are being developed in America cannot be economically used in this country . . . because existing British plants produce more rapidly than the products can be disposed of." When Mr. Armitage says that machines cannot be used "economically" he means that they cannot be used profitably. He means, precisely, that in British conditions a

smaller, instead of a larger, amount of profit would be produced for the British motor-car building capitalists if they accumulated sufficient capital to scrap their present machines and to instal the new and superior American machines. Accordingly they refrain from this act of accumulation and carry on production on the older, smaller basis. They would be very foolish if they did anything else.

We know, however, that just this refusal, however inevitable it may be, to carry on accumulation at the maximum rate must at once produce, as it has done in Britain, the simultaneous appearance of masses of unemployed labour and masses of unemployed capital: must, in a word, usher in the period of permanent, although fluctuating, capitalist crisis. The *Automobile Engineer*, however, tells us that "the time has now arrived when Mr. Armitage's remarks may be widened to a statement that the latest machine tools now being developed in America cannot even be economically used in the United States "

What was a special condition of British capitalism has now become a condition common to capitalism everywhere. *It actually has become more profitable for capitalism, in some cases at any rate, to refrain from accumulation than to accumulate.* The last chapters will have shown us the fatal importance of this conclusion. To apply Engels' words, the historical mission of capitalism in the automobile industry was the ruthless development of those more and more wonderful machine tools which enabled the miracles of modern mass automobile production to be accomplished. And capitalism developed these more and more wonderful machine tools because it was profitable for it to do so. Now, however, it has become, or is becoming, unprofitable for it to take another step in advance. "It becomes disloyal to its mission whenever it puts a check upon productivity as it does here."

Finally, the *Automobile Engineer* goes on to enquire whether there is any remaining market for these latest, super-efficient machine tools, the use of which has now become impossible, because unprofitable, in America as well as in Britain. Pat comes the *Automobile Engineer's* answer. Yes, there is one remaining market for these super machines: there is one place

on the earth's surface where men can use for their own advantage the beautiful and marvellous achievements of the technicians,

“ American machine tool makers having a range of equipment sufficient to meet the needs of the American production plants have supplied to Russia machine tools outside this range, specially designed to obtain still faster production.”

In the U.S.S.R. the dilemma of profits or plenty has been solved in the only way in which it can be solved, namely by eliminating profits. In the U.S.S.R. plenty can be, and is now being, directly built up by means of productive methods which, it is true, will not yield a profit to anybody, but which are undertaken none the less for that. “ The means of production ” have become, in Marx's words, “ mere means for an ever expanding system of the life process for the benefit of the society of producers.” Those superb new means of production with which science has furnished us can at last “ steer straight towards an unrestricted extension of production ” : for the barrier “ of the limited end of the self-expansion of the existing capital ” has been swept aside.

#### SUMMARY OF CHAPTER XIX

We have now seen how recovery is aided by the destruction of constant capital. Modern improvements in the methods of this destruction render Marx's description of it quite out of date. Surprising failure of his capitalist critics to point this out.

A reduction of real wages also necessary, however, to secure recovery. This is an appropriate measure to restore profits, but an inappropriate measure to increase consumption. We come back to the profits or plenty dilemma of Part I. The very measures which make recovery possible ensure the coming of the next crisis by cutting down the market. Capitalism surmounts one barrier by setting another and higher barrier a little further along its path. The ever growing contradiction between the ever lengthening structure of production (to regress to Dr. Hayek) and the permanently minimal basis of consumption becomes



more and more intolerable. The Hayek-Robbins solution reconsidered. Production exclusively for a market within the structure of production. The necessity for augmenting the output of consumable goods, and so of providing a market for them, thus avoided. The logic of insanity. The system does not work like this. It is not merely a misdirection of investment.

Moreover the point comes when the continued development of society's power of production comes into conflict with capitalism's end, the maximization of profit.

What should be our end, namely the production of use values for our sustenance and enjoyment, becomes under capitalism our means. What should be our means, *viz.*, the development of society's powers of production, becomes under capitalism our end.

Palme Dutt's citation of a particular example of capitalism's present inability to derive profit from, and so to use, the latest developments of technique. The latest machine tools in the automobile building industry become unusable first in Britain. Now they are unusable in America and throughout the capitalist world. But they can be used, and are being used, in the U.S.S.R.

## CHAPTER XX

### *The Secret of Money*

It remains to assess the real importance of money in the prevention or precipitation of capitalist crises.

We are now in a position to realize the limited importance in contemporary conditions of the debate between the inflationist and the deflationist schools of capitalist economists. That debate, we discovered in Part I, turned on the question of which was the best way of restoring the rate of profit. We have now come to the conclusion, however, that it has become impossible to sustain the rate of profit at a tolerable level except for relatively short intervals. Besides this conclusion the soundness or unsoundness of the different ways in which the attempt is made to restore that rate pale into relative insignificance.

This, however, is not to deny the validity of the contention of Dr. Hayek and his school that the inflationary method of raising prices is more unsound, will produce a new crisis more rapidly, that is to say, than will the orthodox method of reducing money wage rates and cutting social services, etc. Moreover, this essentially minor consideration is lent practical importance to-day by the fact that the present recovery has been engineered, and can be sustained alone, by methods far more inflationary than any which have ever been applied before. For, as we showed in Part I, the whole American Recovery programme is inflationary to an extent which even its sternest critics seldom realize.

In order to assess quantitatively the importance of this monetary factor we shall now examine the very real part played by money, and by monetary policy, in the actual precipitation of crises.

Marx fully accepted the view that an "expansionist" monetary and credit policy (to use current terminology) was totally unsound, in the sense that it would increase the frequency and violence of capitalist crises. Or rather Marx did not accept this conclusion: he enunciated this conclusion some forty years before Dr. Hayek and his friends rediscovered it. The fifth and sixth parts of Vol. III of *Capital* remain the definitive account

of the effects of the development of a credit system upon capitalism.

Marx traces the development of a credit system from the growing use of money as a means of payment, and from the economies which can be effected by balancing a chain of such payments against each other in a clearing house.<sup>1</sup> He shows that such a development is an integral and necessary part of the development of the capitalist system. Capitalism could never have progressed beyond the stage of quite small scale production without the development of credit. But, at the same time, this development seriously increases the instabilities of the system. For, Marx shows, it progressively blinds the producers and dealers to the real state of the market. They are enabled by credit to go on with their transactions for some time after it would have become clear, if only cash was being used, that disproportions between various lines of production had developed, or, worse, that the rate of profit over the whole economy had fallen to a level where further accumulation was unprofitable. Hence a credit system allows the capitalists to postpone adjusting their system to the real situation. Naturally, therefore, it makes the necessary adjustments more violent and painful, makes them into crises, when in the end they have to be made.

This was almost exactly what, as we discovered in Chapters V and VI, Dr. Hayek's theories amounted to in the ultimate analysis. He, too, concluded that it was the impossibility of achieving "a neutral money," which would passively mediate the exchange of commodities, which made it inevitable that the true direction of demand should become distorted, and the producers be correspondingly misled.

In particular, he criticized any attempt to reduce demand at the consumers' end of the structure of production, and expand it at the producers' end, by the inflationary method of lending the producers of producers' goods new money, instead of by first taking the money from the consumers by wage cutting. He considered such an attempt unsound because of the tendency of new money to percolate down the structure of production until it came into the hands of the individual consumers. This is the

<sup>1</sup> Hence Bills of Exchange are the historically primary credit instruments.

essence of Dr. Hayek's criticism of inflation. His complaint is that inflation fails to impoverish the individual consumers effectively and permanently, and so permits a recrudescence of demand at the bottom of the structure of production. We can now link this conclusion with the undeniable tendency, visible during every period of capitalist expansion, for investment to take place throughout the structure of production instead of being confined to its upper reaches. For, Dr. Hayek would no doubt allege, it is the reappearance of an increased demand for consumers' goods which tempts the investors to create that flood of new consumers' goods which appears on the eve of the crisis. But we shall remain entirely sceptical of the possibility of preventing, even by the most heroic deflation and wage cutting, this general growth in productive capacity from including in its latter stages a marked growth in the capacity to produce consumers' goods. And, as we saw in the last chapter, it is this phenomenon which brings on the crisis, for it reveals the fact that there exists, and can exist, no market for an addition to the supply of consumers' goods.

Marx analyses the central rôle played by credit in the evolution of the early nineteenth century type of genuinely "private" capitalism into modern large scale capitalism dominated by "public" corporations. Marx sees credit as the great agent of mergers, as the device by which the vast aggregates of capital necessary for modern productive methods can be assembled without doing away with the principle of private ownership. But this advance is only accomplished at a price. The growth of credit

"establishes a monopoly in certain spheres and thereby challenges the interference of the state. It reproduces a new aristocracy of finance, a new sort of parasite in the shape of promoters, speculators and merely nominal directors; a whole system of swindling and cheating by means of corporation juggling, stock jobbing, and stock speculation. It is private production without the control of private property." (*Capital*, chap. xxvii, p. 519.)

Thus credit enables the capitalist system to transcend the barrier to the development of large scale production which would

be imposed if it were impossible to pool the capital of different individual capitalists. But it only does so at the cost of decreasing the stability of the system. The development of credit favours and fosters the rise of a new type of capitalist. The most successful capitalists assume "more and more the character of pure adventurers." The old, sober, cautious type of capitalist who owned and operated his own individual lump of capital, embodied in his own factory, or his own steamships, gives way to slick manipulators of blocks of borrowed or, for that matter of purloined, capital.

Marx sums up this process as follows :

"The credit system appears as the main lever of over-production and over-speculation in commerce solely because the process of reproduction, which is elastic in its nature, is here forced to its extreme limits. And it is so forced for the reason that a large part of the social capital is employed by people who do not own it and who push things with far less caution than the owner, who carefully weighs the possibilities of his private capital, which he handles himself. This simply demonstrates the fact, that the production of values by capital based on the antagonistic nature of the capitalist system permits an actual, free, development only up to a certain point, so that it constitutes an immanent fetter and barrier of production, which is continually overstepped by the credit system. Hence the credit system accelerates the material development of the forces of production and the establishment of the world market. To bring these material foundations of the new mode of production to a certain degree of perfection, is the historical mission of the capitalist system of production. At the same time credit accelerates the violent eruptions of this antagonism, the crises, and thereby the development of the elements of disintegration of the old mode of production.

"Two natures, then, are immanent in the credit system. On one side, it develops the incentive of capitalist production, the accumulation of wealth by the appropriation and exploitation of the labour of others, to the purest and most colossal form of gambling and swindling, and reduces more and more the number of those, who exploit the social wealth. On the

other side, it constitutes a transition to a new mode of production. It is this ambiguous nature which endows the principal spokesmen of credit from Law to Isaac Pereire with the pleasant character of swindlers and prophets." (*Capital*, Vol. III, chap. xxvii, p. 522.)

The pleasant company of swindlers and prophets has received many and notable recruits since Marx's day. The line now stretches from Law to Kreuger, to Harrison, to Hatry, to Stavisky. It must be admitted, however, that our contemporary credit manipulators have had more of the swindler proper and less of the prophet about them than had their earlier prototypes. Law and his like did genuinely dream of a Utopia for all as well as a fortune for themselves. Your modern crook is more prosaically sordid.

It is the development of the credit system, then, which allows capitalism to overstep for a season the barrier which its necessity to minimize the consuming power of the population (in order to sustain the rate of profit) creates for it. Credit, says Marx, allows the capitalists and merchants to extend their sales "far beyond the demands of society" (far beyond the demands of society as limited, that is to say, by capitalism's need to keep some four-fifths of society down to subsistence level). But then, of course, the system must pay for this artificial extension by an equal and opposite contraction. For the account must balance in the end. If this year you have sold by means of credit (on the hire purchase system, for example) more goods than people had money to pay for, you can next year sell even fewer goods than people have money to pay for. For some of their money will have to be used to complete the payments for this year's goods. (This little arithmetical truism is regularly forgotten in every boom.) Credit makes the cash nexus which unites the dealers of an exchange economy into an elastic nexus. It allows production to swing out beyond the limits imposed upon it by the social system. But then, and to the same extent, it pulls production in within those limits.

If we can imagine a creditless capitalism in which every transaction was mediated by hard cash, then it is true that the oscillatory form of the crisis, but not the crisis itself, might be

abolished. We should get a slow, steady decline of the rate of profit which would act upon the system like a creeping paralysis. This is the kind of situation towards which Dr. Hayek and his school would have the system approximate. An absolutely fixed circulation of money (for which Dr. Hayek longs so wistfully) would take the system, were it attainable (which he agrees it is not) some way towards this condition.

These considerations as to the effects of the development of credit upon the stability of capitalism lead Marx towards an elucidation of the nature of money itself.

"It is a basic principle of capitalist production," Marx writes, "that money, as an independent form of value, must stand opposed to commodities, or that exchange-value must assume an independent form in money, and this is possible only by the making of one definite commodity the material, whose value measures all other commodities, so that it thus becomes the general commodity, the commodity *par excellence* as distinguished from all other commodities." (*Capital*, Vol. III, chap. xxxii, p. 606.)

Capitalism imperatively requires, that is to say, some objective embodiment of value, with which it can compare the magnitude of the values of all other commodities. This necessity, Marx proceeds to show, explains why it is that the capitalists are so loth, and from their point of view are rightly loth, to break the convertibility of their paper money with the objective standard of value; why they are so loth, as we should say, "to go off the gold standard." It is often the case (*viz.*, Germany, or France, or Holland in 1934) that a capitalist crisis would be enormously eased by a depreciation of the credit money in circulation. For it is politically much easier to reduce real wages, etc., by raising prices than it is to reduce the money rates of wages. But it may be observed that experienced capitalist Governments, and more especially those which have had a recent experience of depreciating their credit money, will do almost anything to avoid a second trial of this expedient. We have already given Dr. Hayek's explanation of this. Marx explains it more simply, and more profoundly, by showing that any tampering with the

actual standard of value, "the independent form of value which must stand opposed to commodities," is apt to throw a capitalist economy into confusion. Rather than risk this confusion, a drastic writing down of the prices of all commodities including labour power is preferable.

But what does this revelation of money as the independent existence of value mean? It means that money *is* the unconscious expression, the fetish, to use a modern term (but one which Marx employs) of the social character of labour. "The social character of labour appears as the money-existence of commodities," writes Marx. He means that under capitalism the only way in which the fact that we are all dependent upon each other's labour can be expressed is that the tangible or intangible results of our labours should all be exchangeable one with another, by being all and each exchangeable with money.

The secret of money is, then, that it is the unconscious, fetishistic, expression of the social character of wealth. For under capitalism, which is based on the private individual ownership of wealth, the fact that wealth has become, with modern large-scale productive methods, almost completely social as opposed to individual, both in the manner of its creation and to a large extent even in the manner of its enjoyment, can only find expression in an unconscious, mystified way. Engels in one of his interpolations puts the point in this way. He says that under capitalism,

"the wealth of society exists only as the wealth of private individuals, who are its owners. It shows its social capacity only in the fact that these individuals exchange the qualitatively different use-values mutually for the satisfaction of their wants. Under capitalist production they can do so only by means of money. Thus the wealth of the individual is realized as a social wealth only by means of money. In money, in this thing, the social nature of this wealth is incarnated." (*Capital*, Vol. III, chap. xxxv, p. 673.)

The capitalists do not consciously recognize that their wealth is social. A contemporary rich man does not realize that the, say, £500,000 which he owns is not absolute individual wealth at all. He does not admit to himself that the enjoyments, powers



and privileges which he gets out of the ownership of this wealth are wholly dependent upon the continued existence and proper functioning of the complex and infinitely interrelated productive system. We have studied in all the preceding chapters the conditions necessary to the functioning of this system on a capitalist basis. It was necessary, we found, that both certain proportions between the total rate of accumulation and the rapidity of the fall of the rate of profit, and certain proportions between the different departments of production, should be preserved. And in order that these conditions should be preserved, and the system continue to function, it is imperative that an objective, independent, standard of value, which incarnates socially necessary labour time, and so enables commodities to be added up and compared, should be preserved inviolate—although the true nature of this standard is unperceived or denied. For when Marx and Engels say that in money the social nature of wealth and exchange value are incarnated, they mean that money is the embodiment, the incarnation, of socially necessary labour. Money is, then, the fetish, or mystified incarnation, of that common factor in commodities which we isolated as socially necessary labour.

The capitalists do not recognize all this when they think. They do not know it consciously. They deny that money incarnates socially necessary labour, they try to ignore the social character of wealth. But they do know all this when they act. They know it unconsciously. They know it as a result of frequent and painful experience. This explains the peculiar sanctity with which an objective monetary standard is endowed. This explains the awe in which the gold standard is held. The gold standard is often called a fetish by its capitalist opponents. They are right. It is a fetish. But have they considered the nature of fetishes? Fetishes are not empty idols. They are unconscious, mystified expressions of deep needs. And so it is with the gold standard. The gold standard is the fetishistic expression of the absolute need of capitalism for an incarnation, an unconscious, automatic and objective expression, of the factor common to all commodities, which alone renders them commensurable, *viz.*, socially necessary labour time.

Moreover, the capitalists are perfectly right, from their point

of view, to worship their fetish. Once destroy, finally and completely, the objectivity of money and there would remain no nexus between producers. Wealth would lose its social character; commodities would no longer be exchangeable. Capitalist society would dissolve.

If we wish for confirmation of this view, we have but to look around us at the world of 1934. The storm of the great depression was sufficiently violent to force several of the great capitalist states (*viz.*, America, Great Britain, and Japan, plus a host of smaller states) to rupture the convertibility of their credit money into gold, in order to depreciate this credit money, and thus raise the prices of all commodities, or, at any rate, to arrest their fall. For thus they were enabled to raise the rate of surplus value without the painful and politically dangerous process of slashing money wage rates. These states took the apparently easier path. It is not too much to say that their action went far to disrupt international society—to disrupt capitalism as a world-wide entity. The international movement of capital was completely interrupted and has hardly been resumed. The movement of commodities was reduced to about a third. And that the consequences were not even greater is largely due to the fact that one block of states, at any rate, did retain the convertibility of their credit money into gold. It is true that the capitalist societies which ruptured convertibility were not disrupted internally. Some of them, however, came towards the breaking point. Moreover, it was, and is, precisely this fear of the dissolution of the most essential bonds of an exchange economy which has so far forced (November 1934) the German capitalists to refrain at all other hazards from again resorting to depreciation.

In Great Britain the internal bonds of the economy were not broken by the rupture of convertibility because what Marx calls "the social character of production" was never very seriously called into question. The faith of the population in its medium of exchange as an effective means of purchase and payment held good. But, in the midst of a crisis, and more especially if convertibility has been ruptured, this act of faith becomes necessary to the survival of the economy. For what does faith in the social character of production mean? It means that the

producers and dealers believe that the commodities which they are producing, or buying and selling, will fetch a price, and will fetch a price not too ruinously below their expectations. But the condition of commodities fetching a price is that there has been some rational proportionality between the different lines or departments of production, and that production as a whole has not outrun the total demand of the population as limited by the nature of capitalism. But how can the producers and dealers discover whether or not these conditions have been fulfilled? They can only do so by the acid test of each and every producer and dealer actually selling the commodities which he has produced or is holding.

It is this which constitutes the danger of the position. For once a gnawing doubt as to whether, in fact, one's commodities can be sold : as to whether they can be converted, that is to say, into money, and in particular into a reasonably adequate quantity of money : once this doubt has arisen, then the only way in which it can be allayed is to put the matter to the test ; to sell. Hence a panic rush to sell will occur whenever the outbreak of a crisis has revealed the fact that the elastic of credit has allowed capitalist production to swing out beyond its inherent barriers, and that it must now swing back as far within them. But the panic rush to sell naturally makes everything unsaleable. If every dealer simultaneously attempts to put his commodities to the trial by ordeal of sale, to the *saltum mortale* of commodities, as Marx calls it, then none will pass the test. For it is inconceivable that all of an advanced capitalist economy's vast stock of commodities can be simultaneously converted even into credit money (of which there is normally a large supply). Yet once the horrid doubt has arisen in the breast of a dealer<sup>1</sup> as to whether the particular commodities which he owns *are* socially necessary, as to whether the labour embodied in them *was*, after all, socially necessary labour, he will not be able to sleep until he has put the matter to the test and got the cheque for their sale in his pocket. This was the doubt, rising simultaneously in the breasts of literally millions of American citizens, which in March 1933 broke the topless

<sup>1</sup> Not, of course, that he thinks of the matter in this way. But that is what it amounts to.

towers of New York—or, at any rate, emptied them of all their tenants.<sup>1</sup>

But what if money, what if the very thing into which there is during every crisis so violent a rush to convert commodities, has itself become of doubtful value? What if the dealer begins to doubt the cheque with which he has been paid? And that is just what must necessarily happen to credit money in a crisis sufficiently acute to call into question its convertibility into gold. Just as, so soon as doubts as to the value of his commodities are raised, everyone will rush to convert them into money, so, at the second stage, when doubts as to the value of credit money itself are raised, everyone will rush to convert their credit money into gold. Naturally, however, there is nothing like enough gold available to make this a practical possibility. It is of this second stampede that Marx writes:

“But as soon as credit is shaken—and this phase always appears of necessity in the cycles of modern industry—all the real wealth is to be actually and suddenly transformed into money, into gold and silver, a crazy demand, which, however, necessarily grows out of the system itself. And all the gold and silver, which is supposed to satisfy these enormous demands, amounts to a few millions in the cellars of the Bank.”<sup>2</sup> (*Capital*, Vol. III, chap. xxxii, p. 673.)

Are not the capitalists absolutely right, then, in attempting almost at all costs to protect the convertibility of their credit money? The fetish of the gold standard is a necessity for capitalism. Like other fetishes, however, it demands constant and painful sacrifices. Moreover, *some* of these sacrifices are unnecessary. We have seen that the capitalists only recognize unconsciously that socially necessary labour time is the basic

<sup>1</sup> “As pants the hart for cooling streams,” writes Marx of the dealer in these circumstances, “so does his spirit pant for money, the only wealth” (*Capital*, Vol. I, p. 120.)

<sup>2</sup> Years before Vol. III of *Capital* was published Marx had graphically described this process. “The sudden reversion from a system of credit to a system of hard cash, heaps theoretical terror on the top of practical panic; and the dealers by whose agency circulation is effected tremble before the impenetrable mystery in which their own relations are involved.” (*The Critique of Political Economy*.) The dealers are trembling still. *Vide* Mr. Montagu Norman’s statement during the 1932 nadir of the crisis that he did not pretend to understand what was happening to him.

common factor in commodities which renders them commensurable, and so makes it possible to regulate the proportionalities of the various departments of production, and of production as a whole to effective demand. They recognize it only by the act of erecting as a fetish the commodity gold, to be the nameless incarnation of socially necessary labour time. They do not know why, but they know that terrible misfortunes will befall the tribe if this fetish is tampered with. Hence they sometimes perform unnecessary and meaningless sacrifices to it. Marx believed, and most capitalist economists would now concur, that the provisions of Peel's Bank Charter Act of 1844, by which the excess of the fiduciary issue over the gold reserve of the Bank of England could not legally fall below a certain figure, was a case of this superstitious and irrational sacrifice. But, in the last resort, Marx agrees, this is not a big point. If the capitalists wish to minimize crises, they will take strong action to safeguard convertibility. It is a question merely, Marx writes, of "the more or less rational treatment of the inevitable." Marx has no patience with amiable reformers who suppose that crises could all be cured or avoided if only the banks would issue ever more and ever cheaper credit. He calls them, in a Johnsonian phrase, "fools who believe that it is the destiny and power of banks to transform all bankrupt swindlers into solvent and solid capitalists by means of pieces of paper."

The essentially superstitious attitude of the capitalists towards money is striking. In one of those notes which Engels found in the various manuscript drafts of Volume III, and which, although they were, no doubt, intended by Marx for later elaboration, he wisely included, Marx draws a parallel between a cash money system and Catholicism, and a credit system and Protestantism.

"The monetary system is essentially Catholic, the credit system essentially Protestant. 'The Scotch hate gold.' In the form of paper the monetary existence of commodities has only a social life. It is Faith that makes blessed. Faith in money-value as the imminent spirit of commodities, faith in the prevailing mode of production and its predestined order, faith in the individual agents of production as mere personifications

of self-expanding capital. But the credit system does not emancipate itself from the basis of the monetary system any more than Protestantism emancipates itself from the foundations of Catholicism." (*Capital*, Vol. III, chap. xxxv, p. 696.)

The economical Protestant's faith in the convertibility of money into commodities, and in the convertibility of credit money into hard cash, enables him to effect the substantial economy of making do with a minimum of the expensive precious metal. Hence the North British detestation, not indeed of gold, but of the wasteful use of gold. But this economy is only effected by a vast growth of instability. Alas, that faith even in Edinburgh and Glasgow is sometimes misplaced! Moreover, even apart from swindlers, it has often happened, during the past fifteen years, that the commodities produced on the banks of the Clyde have not been able to stand up to the acid test of sale. It has been discovered that the labour embodied in them was *not* socially necessary labour: that the limits of the capitalistically restricted demands of society had been far transcended.<sup>1</sup>

There is no doubt that Marx discovered the essential nature of money, and so was able to explain and to assess the importance of the money crises which superimpose themselves upon the crises of capitalism. The crises themselves are made inevitable by the ever growing contradictions of the system. *One way of expressing briefly the reason why capitalist crises are inevitable is to say that they come about because it is necessary to minimize the population's purchasing power in order to obtain even a minimal rate of profit on the ever vaster mass of capital being used in production, and to maximize their purchasing power in order to be able to sell the products. And you cannot do both.* But crises occur in their present form of alternating booms and slumps because of the development of the credit system. The crises are anything but monetary. They are rooted in the very nature of the system. But the form of the crises is largely monetary. Boom alternates

<sup>1</sup> It is amusing to notice how a preference for the expensive certainty of hard money does seem to be expressed by the adherents of the Catholic faith. Mr. Hilaire Belloc, perhaps the best known English-speaking Catholic theorist, was only the other day telling us that "the future of Western civilization" depended on the availability and use of a metallic money for the mediation of its transactions.

with slump because the development of the credit system allows capitalism briefly to transcend its barriers, to push production beyond what is, in fact, the profitable point. But this extension is dearly bought. For it means that, when the next crisis comes it will be complicated and heavily intensified by stampedes, first from commodities into credit money, and then from credit money into gold.

Yet for all the noise which they make in the world, and for all their indisputable importance in the day to day run of events, these stampedes, these financial crises, are but the epi-phenomena of crises. And all the prudent proposals of Dr. Hayek, Professor Robbins, and the more conservative central bankers, touch only these epi-phenomena. They might do something (if they were practicable, which they are not), as compared, at any rate, to the reckless inflationism of Mr. Roosevelt, to mitigate the now sickening oscillations of the system, to prevent the damage done by the stampedes of the panicked dealers. But they could do nothing to extricate the system from its basic contradictions.

#### SUMMARY OF CHAPTER XX

We can now assess the importance of the part played by money in capitalist crises. Marx's account of the effect on capitalism of the development of credit. Credit postpones the necessity of adjustments, but makes those adjustments convulsive when at length they have to be made. Similarity of this conclusion with that of Dr. Hayek. Credit changes the nature of the typical, representative capitalist as well as the nature of capitalism. The emergence of the "pure adventurer" type. The pleasant company of swindlers and prophets. Credit makes it possible to sell people more than they can pay for this year, but only at the cost of being able to sell them even less than they can pay for next year. In general credit increases the instabilities and oscillations of the system.

The nature of money. Marx on capitalism's necessity for an independent form of value. Money as this independent form of

value. The capitalists rightly reluctant to tamper with the objectivity of money. Money as the fetish, or unconscious expression, of the social character of labour, and so of the social character of wealth. Engels on the social character contrasted with the individual ownership of modern wealth. Money as the incarnation of that "more fundamental something" which alone renders commodities commensurable. Money, that is to say, as socially necessary labour incarnate. The Gold Standard *is* a fetish. But it is a necessary fetish, essential to the working of capitalism. Wisdom of those capitalists who stick to their fetish. Lessons of the great depression on the devastating effect on international trade of the abandonment of the Gold Standard fetish. Ability of those capitalist economies which ruptured the convertibility of their credit money and gold to preserve themselves from disruption, seen to be dependent upon an act of faith on the part of their citizens.

Their citizens on the whole preserved their faith in the social character of production, their belief that their commodities contained socially necessary labour time. But, whenever that faith is shaken there is bound to be a stampede to sell. For sale, *i.e.*, conversion into money, is the only possible way of putting the question to the test. But what if men's faith, not only in the vendibility of their commodities, but also in their credit money, is shaken? Then there will be a second stampede from credit money into gold. But this stampede cannot possibly succeed. For there is only a trivial amount of gold in the banks with which to satisfy everyone's desire to own gold instead of either commodities or credit money. Thus the capitalists are very wise to make almost any sacrifices to their golden fetish. These sacrifices, being blind, are sometimes overdone : but that is all.

The analogy between Catholicism and hard cash and Protestantism and credit.

Summary of the importance of money in crises. The fact of crisis not in the least due to monetary factors. But the form of the crises, as a series of ever more violent oscillations, is due to monetary factors. The stampedes of the panicked dealers. Financial crises as epi-phenomena. Hence comparatively small importance of the Hayek-Robbins remedial programme.



**PART V**  
**THE THEORY APPLIED**



## CHAPTER XXI

### *The Present Crisis*

ON page 369 of the third volume of *Capital* (and this volume runs to over a thousand pages) Marx remarks that "the reader will have realized to his great dismay that the analysis of the actual internal inter-connections of the capitalist process of production is a very complicated matter and a very protracted work."

Even our exceedingly schematic analysis has taken time to present. Moreover, our analysis has only been kept within the limits of the preceding chapters by the rigid exclusion of anything but the barest essentials. For example, no account has been given of Marx's analysis of how disproportions arise between the different departments of production (and these disproportions may themselves make accumulation impossible). This analysis is contained in the final section of Vol. II. Dr. Hayek's construction is anticipated in this argument. Marx's conclusion that, in order that accumulation may take place, the variable capital plus the surplus value in the producers' goods department of production must exceed the constant capital in the consumers' goods department, is another way of expressing Dr. Hayek's conclusion as to the necessity of cutting down individual, unproductive consumption in order to get a trade revival.

Above all, we have paid no attention to the question of the concentration of capital. Marx describes in detail how step by step with the development of the productive power of labour (the fall of  $\frac{v}{c}$ , as we called it) another process makes itself felt. This is the concentration of capital into larger and larger aggregates; the fusion of many separate individual, independent capitals, operating in competition with each other, into larger and larger and fewer and fewer masses. This process of the concentration of capital has the most important political consequences. It is this process which ushers in that new and distinct stage of capitalist development in which we live, and which Marxists call "monopoly capitalism" or "imperialism."

It was this development which formed Lenin's special field of study.<sup>1</sup>

The study of monopoly capitalism as such must, in one sense, begin where this book leaves off. Our argument stops when we have established the essential nature of capitalism itself. We do not deal with the question of the extent to which this nature has been modified by the growth of monopolistic forms. This may make the reader feel that there is something abstract about the thesis of these pages. For they do not deal, except in the concluding chapters, with the partition and repartition of the world ; with the question of the degree to which monopoly can postpone for a time the tendency of the rate of profit to fall ; with the degree to which the growth of monopoly intensifies the severity of that fall when it occurs ; with the degree to which monopoly prevents recovery by impeding the elasticity of the system ; with the degree to which recovery is blocked by the exclusive imperialistic possession of remaining undeveloped parts of the world ; and finally with the loss of one-sixth of the world (the U.S.S.R.) as an area for capitalist investment.

It seemed useful to devote one book to emphasizing Marx's analysis of capitalism in its basic, competitive form. For imperialism, or monopoly capitalism, has not so much abolished competition as modified the methods by which competition is carried on. Competition is still the general rule of the system. The degree to which competition has been suspended within each national economy is often exaggerated ; while international

<sup>1</sup> The existence of this process of the concentration of capital is sometimes denied. It is said that the modern trust does not represent a concentration of capital because its capital is owned by a large number of small shareholders. The objection is based, like so many others, on an ignorance of what it was that Marx said. Marx was not thinking, primarily, at any rate, of a concentration of the ownership of capital. He was thinking of the actual pooling, for technical purposes, of the numerous individual and hitherto competing capitals of a number of independent firms which takes place when a trust is created. This represents a stage in the concentration of capital, even although some of the shares of the new trust are held by a good many individuals, perhaps even by as many as had shares in the independent firms before they were merged. For the crux of the matter is that the number of independent, competing, productive units operating on the market has been drastically reduced and so monopoly conditions approximated to, or even in some cases reached.

Marx, however, claimed that this concentration of capital into ever fewer and ever larger units, was associated with a concentration of the effective control, and ultimately of the ownership, of capital into fewer and fewer hands. Nor will anyone who has the slightest knowledge of the tendency of the distribution of wealth in the leading capitalist countries be able to deny that he was right.

competition, though now carried on by more and more openly violent methods, has actually been intensified. Hence the basic law of motion of the system which Marx discovered remains in full force. And until we have fully grasped the nature of Marx's discovery, we cannot pass on to Lenin's application of that discovery to the specific conditions of our day. For the whole growth of monopolistic and imperialistic forms within present-day capitalism is itself the direct consequence of the working out of Marx's law of motion of competitive capitalism. Lenin's analysis is deeply rooted in Marx's definitive revelation of the nature of capitalism itself; we are certain to misinterpret Lenin unless we have first fully comprehended Marx.

Thus the reader of this book must on no account suppose that he has obtained a complete or balanced picture of the workings of the capitalist system. In order to get a grasp of the full nature of capitalism, a serious study of the works of Marx, Engels, and Lenin is indispensable. An exclusion of important elements even in Marx's account of capitalism, to say nothing of Lenin's analysis, can only be excused on the ground that it was useful to have one study devoted exclusively to the analysis of capitalist crisis. Yet in the press of events which in our epoch crowd upon us some of those who are already convinced of the decay of capitalism may be tempted to think that Marx's crisis analysis is not of the first importance. What, after all, does it tell us, they may object, except that capitalism is subject to periodic, ever worsening, and now chronic crises? And, in order to learn this, we have but to look around us. An attitude of indifference to Marx's theory of crisis has, indeed, been widespread, even in the working-class movement, and even in working-class parties avowedly based upon Marxism.

In this Part we shall endeavour to show the extreme importance of that understanding of the essential nature of capitalist crisis which a comprehension of Marx's crisis analysis alone can give.

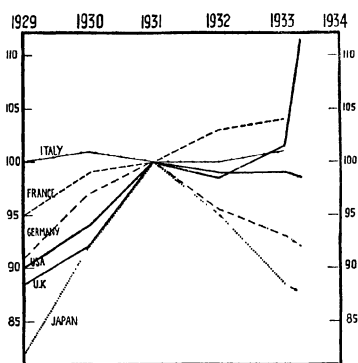
What symptoms should we expect to discover in the years immediately preceding the outbreak of an acute crisis if Marx's analysis is correct? The cause of crisis, Marx wrote, was the fact that the productive power of capitalist society was

continually growing, while the ultimate market for which the system worked could hardly be expanded at all. Therefore the market, "the basis" (Marx uses this term) of the whole structure of production was getting smaller and smaller, *relatively to the length of that structure*. (See Vol. III, pp. 312-13.)

But Marx did not suggest that there was any tendency for this basis (the ultimate market provided by individual consumption, that is to say) to contract absolutely. On the contrary, Marx has a significant passage in Vol. II in which he recognizes that just before the outbreak of crises this ultimate market grows a little. In this passage he deals faithfully with the ordinary, grossly over-simplified, under-consumptionist explanation of crisis.

"It is," he writes, "purely a tautology to say that crises are caused by the scarcity of solvent consumers, or of paying consumers. But if one were to attempt to clothe this tautology with a semblance of a profounder justification by saying that the working class receive too small a portion of their own product, and the evil would be remedied by giving them a larger share of it, or raising their wages, we should reply that crises are precisely always preceded by a period in which wages rise generally and the working class actually get a larger share of the annual product intended for consumption. From the point of view of the advocates of 'simple' (!) common sense, such a period should rather remove a crisis. It seems, then, that capitalist production comprises certain conditions which are independent of good or bad will and permit the working class to enjoy that relative prosperity only momentarily, and at that always as a harbinger of a coming crisis." (*Capital*, Vol. II, p. 476.)

Thus Marx clearly recognizes that a crisis is usually preceded by a rise in real wages, and that this rise is "a harbinger" of the coming storm. How do the facts of the great depression of 1929 tally with these expectations? The most convenient summary of the situation is to be found in a chart showing the movement of real wages in various countries, published by the London *Economist* in the issue of June 2nd, 1934, and here reproduced by courtesy of the Editor.



The reader will notice at a glance that in every country cited, with the exception of Italy, real wages were rising during the latter period of the boom and in the early period of the depression.

The author of this chart affixed the following explanation of it.

“The downward movement of the trade cycle between 1929 and 1932 was accompanied by a profound disturbance of relative prices, reflected in growing unprofitability of most forms of activity and in increasing unemployment of factors of production. Efforts to stem the narrowing of the margin between costs and selling prices and to increase competitive efficiency at home and abroad involved drastic reductions in costs of production, of which labour is the most important single element. Money wages, therefore, suffered reductions of greater or less extent in all parts of the world. But to a varying extent these were offset by changes in the cost of living. It is, therefore, of particular interest to examine the Wc

movements of real (as opposed to money) wages in the leading industrial countries since 1929. The index numbers of real wages, shown in graphical form above, were obtained by application of official indices of the cost of living to the indices of wage rates published in the *International Labour Review*. The results are not strictly comparable, for the figures for France, Germany, Italy, and the United States are based on hourly wage rates, whereas those for Japan and the United Kingdom are based on daily and weekly wage rates respectively. Moreover, it should be borne in mind that the chart has been compiled on the basis of published wage rates, which, owing to the prevalence of 'short-time' or 'work-sharing' schemes, give little indication of actual weekly earnings."

In basing any conclusions upon this chart the limitations in the statistics from which it is drawn must be very carefully borne in mind. In particular, the fact that the lines representing real wages in France, Germany, Italy, and the United States are based on hourly wage rates alone makes them, in the conditions of recent years, most unreliable guides to the real incomes of the wage earners. Thus the towering rise of the line representing American real wages is in flat contradiction to all the other evidence of what happened during 1933 to the earnings of the American workers. For example, the American Federation of Labour's monthly survey for May 1934 shows that the real *weekly* earnings of American workers failed to rise appreciably between March 1933 and March 1934. A gain of 9.7 per cent in money receipts was almost wholly offset by a rise of 9.3 per cent in the cost of living. More striking, however, because they come from an official apologist of the New Deal, are the figures given by Mr. Donald A. Richberg in his report to Mr. Roosevelt issued on August 27th, 1934. Individual workers' wages only increased by 8.5 per cent while the cost of living rose by 9.6 per cent, between June 1933 and June 1934. Thus real wages actually dropped appreciably, by 1.1 per cent, that is to say. This startling discrepancy is partly explained by another chart which appears in the same issue of the *Economist*. It shows that the average number of hours worked per week in America was dropping sharply during the greater part of 1933.



So long, however, as we are alive to these serious limitations, the chart is undeniably instructive.<sup>1</sup> Here is its author's comment on the upward movement of real wages, of mass purchasing power, that is to say, which the chart shows to have taken place in the years 1929-31.

"In all countries, with the exception of Italy, real wages (and earnings of those in full-time employment) recorded a substantial increase between 1929 and 1931 as prices were falling fast. But as this fall was not accompanied by a corresponding reduction in wage rates or in labour costs per unit of output, it was bound to diminish the number of human and other factors of production which could be employed at a profit, and to lead to an enormous increase in unemployment of men and machinery."

Thus we see that the 1929 crisis was preceded by an increase in real wages. This increase would not, however, be any proof of a net growth of the market, since it might be more than offset by a growth of unemployment. Some interesting statistics presented by the Harvard School of Business tend to show, however, that the consumption of consumers' commodities actually did rise in America all through 1930 and 1931, the first two years of the slump, and was only checked in 1932.

Here is a table, reproduced by Professor Robbins on p. 70 of *The Great Depression*:

INDICES OF CONSUMPTION  
(1928=100)

Article	1928	1929	1930	1931	1932
Wheat flour . . .	100	100.2	101.0	94.5	90.0
Butter . . .	100	101.5	101.8	104.4	105.6
Cheese . . .	100	93.2	99.3	113.2	107.3
Gasolene . . .	100	113.4	120.2	122.8	113.2
Cigarettes . . .	100	112.4	112.9	107.1	97.8
Silks and velvets . . .	100	94.5	98.2	98.3	90.6
Hosiery . . .	100	109.8	118.6	138.8	137.6
Infants' wear . . .	100	107.5	106.8	105.4	91.4
Popular-priced dresses . . .	100	113.5	115.3	125.5	117.7

<sup>1</sup> Another important qualification to the chart is its scale. The reader will notice that the base of the vertical scale would come some way below the bottom of the page. Thus the movements of real wages are made to look more rapid than they actually have been.

These figures indicate that the closing stages of the boom and the first two years of the slump were marked by an appreciable growth in the absolute magnitude of the market for ultimate consumers' goods. It was not until the mass unemployment of 1932 set in, that the market began to contract absolutely.

It seems clear, then, that the crisis of 1929 was not due to any sudden failure in consuming power. What was it due to then? It was due to the emergence in an inescapable form of capitalism's basic dilemma of profits or plenty. It was due to the fact that capitalism could do one of two things. Either it could cut wages and social services and so maintain the profitability of production. But in this case it destroyed the market for the ever increasing supply of consumers' commodities which were coming on to that market. Or capitalism could allow real wages and social services to rise and so provide a market. But in this case it destroyed the profitability of production by depressing the second determinant of the rate of profit, *viz.*, the rate of surplus value.

So much is certain. We now come to the interesting question of which horn of this dilemma in fact impaled capitalism in 1929. And here I for one do not pretend to be able to give any confident opinion. The reader will see that it would not be difficult to make out a case for the view that the 1929 crisis was not caused, in any immediate sense, by a deficiency of consuming power at all, but by a failure of the profitability of production. Further, it might be argued that the proximate cause, "the harbinger," of that collapse of profitability was precisely the enlargement of consuming power which took place in 1929-30. Moreover, it could be argued that the continuing downward swing of the slump was due to the fall of the second determinant of the rate of profit, to a fall, or, at any rate, to an arrest of the natural rise, of the rate of surplus value: that it was due to a failure on the part of the capitalists to cut money wages fast enough to prevent real wages from rising.

Can it be that that hypothetical limiting factor of accumulation having run ahead of the growth of population, and so having bid up the price of labour power above its value, which we considered in Chapter XVIII, did come into play, at any rate in America, in 1929?

Such a conclusion seems to be in direct conflict with the situation in Great Britain, where unemployment never fell below one million. It will be noticeable, however, that British real wages did rise in this period. It may be that the combination of a relatively extensive system of social insurances, and a relatively great trades union strength, were able in Britain to prevent that fall in money wages, and that holding down of real wages, which the height of unemployment would naturally have compelled. For present-day social and political conditions in capitalist "democracies," enforcing "advanced" social legislation, make more probable the precipitation of crisis by way of a failure to hold down real wages, and so maintain an adequate rate of accumulation, than in Marx's day. The political and industrial strength of the working class has after all grown considerably, in spite of everything. The rate of wages paid to those workers who remain in employment has probably in some cases exceeded a true subsistence level. (For it must be remembered that in modern conditions of ever falling costs and prices money wage rates have to be persistently cut in order to keep real wages down to subsistence.) Governments have been compelled to impose considerable taxation upon the capitalist class in order to maintain the unemployed. And this money also constitutes a drain upon funds otherwise available for accumulation.

Moreover, these two drains on funds otherwise available for accumulation are notoriously closely bound up with each other. It is the existence of payments to the unemployed which enables the trade unions to prevent money wages being continually cut as prices fall. Anyone who has ever sat in a capitalist Parliament will have had this fact very forcibly brought home to him by the passionate need felt (and rightly felt, from their point of view) by the capitalist politicians to cut down all "doles" to the unemployed at any cost in human suffering. For they have an instinctive knowledge that any increase in doles to the unemployed may be ruinous to their system, not because of the actual charge on the Budget, which could often be carried quite easily, but because of the fatal increase in bargaining power which doles to the unemployed give to the employed workers.

In America during the great boom of 1924-9, there is some reason to suppose that, probably for the first time and certainly

for the last time in the history of capitalism, the rate of accumulation outran the supply of available labour power, bid up its price, and so reduced the rate of surplus value as to hurtle the rate of profit, already tottering from rapid rationalization, over a precipice. This impression is borne out by the following reflections. The growth of population in America was slow; the flood of immigrants which had for generations supplied ever new material for the exploitation of the American capitalists had been (with incredible folly from a capitalist standpoint) cut off. In spite of trade union weakness and the absence of social services, wage rates for the skilled workers in America had risen to unprecedented heights. Unemployment was as near non-existent as it ever can be under capitalism.

Hence the rate of wages rose in many industries to well above the subsistence level, viz., the level which would serve to provide a continuing supply of labour of the required degree of skill and education. In Marxian terminology, the price of labour power rose above its value. This at once set up a grave disturbance of the system. Rationalization, the fall of  $\frac{v}{c}$ , was hastened till it reached an unparalleled rapidity. For, it is important to notice, a hastening of the fall of the first determinant of the rate of profit, of  $\frac{v}{c}$ , is itself an inevitable consequence of any tendency for the rate of wages to rise above the necessary minimum. For if wages are kept down to the bed-rock of subsistence, the progress of technical change will be retarded. But if wages rise, it will pay the capitalists to introduce labour-saving machinery at an unparalleled speed.

Professor Robbins attaches great weight to this factor as the cause of the 1929 crisis, particularly in the case of Germany. There trade union strength and the social legislation of the Weimar Republic kept wages up in spite of heavy unemployment. Hence rationalization took place on an almost fantastic scale. The bottom fell out of  $\frac{v}{c}$ . In the case of America, also, rationalization was hastened by high wages for some workers. Thus the rate of profit was not being sustained by a counterbalancing growth of the rate of surplus value. The inflationary maintenance of the price-level, which necessitated a vast extension of the elastic of credit, was able to conceal for a while the fatal nature of this situation. But it could do so only at the

expense of making the crisis doubly catastrophic when the continuing fall of the rate of profit broke through all restraints in October 1929.

These features of the pre-slump American situation gave rise to those fantastic economic fallacies with which the world was regaled during the nineteen-twenties. It is difficult (and for their dupes it must be painful) to remember that at that time we were all assured that an entirely new form of capitalism had been discovered. Its father and prophet was Mr. Ford. Economic science from Quesney to Varga, of the classical, marginal utility, equilibrist or Marxist schools, was all alike bunk. The "practical genius," by which expression semi-illiteracy is usually denoted, of Mr. Ford had proved that it was possible for the capitalists to make unheard-of profits and for the workers to earn unheard-of wages, and for this rising harmony to continue for ever. Industrialists and bankers, trades union officials, publicists and priests all enunciated this comfortable gospel. It is remarkable to remember how far to the political Left a faith in "Fordism" or "the doctrine of high wages," as the gospel was usually called, at one time extended. Even the theorists and propagandists of the British Independent Labour Party were found to believe that Marx had been outmoded by Ford, and that undeniable troubles at home were due merely to the failure of European capitalists to come up to the enlightened level of their transatlantic colleagues.<sup>1</sup> It is not too much to say that the revolutionary Marxist economists such as Varga and Dutt alone kept their heads. They alone saw the extreme instability of the American boom, realized that Marx's analysis, far from being disproved, was being exemplified on the most gigantic scale, and, what is more, prophesied the coming collapse. (See p. 359.)

Do we then argue that the 1929 slump was caused, not by an insufficiency of consumers' purchasing power, making it impossible for the capitalists to sell their products, but by an excess of consumers' purchasing power, making production unprofitable? We do not. To do so would be to fall into an equal and opposite error to that of the under-consumptionists. It is of

<sup>1</sup> Mr. Lewis Corey in his *Decline of American Capitalism* has made a fine collection of these fatuities. Mr. Corey's book unfortunately appeared too late for me to discuss his extremely interesting analysis in these pages.

the nature of capitalism's present dilemma that consumers' demand may be *simultaneously* too low to provide a market, and too high to allow of profitable production. This is what Marx meant when he spoke of the contradictions of capitalism. To suggest, as do Professor Robbins and Dr. Hayek, that the slump was simply a collapse of profitability, and to imply therefore that it need never have taken place if only "demand at the consumers' end" had been sufficiently reduced—if only, in plain language, wages had been sufficiently cut—is to ignore the most obvious characteristic of the slump, namely, the gigantic glut of consumers' commodities. The Robbins-Hayek specific would itself have precipitated the crisis by still further contracting the ultimate market.

The truth of the matter may well be that that rise of real wages and consumers' demand which took place in 1929-30 was at the same time inadequate to prevent the glut, and was sufficient finally to destroy the profitability of production. For there is no guarantee that a small increase in the market will prevent the outbreak of a crisis of glut. If the system's productive capacity for consumers' goods, and, in the last stage, the actual production of consumers' goods, is growing with the rapidity with which it grew in America in 1929 (recollect the example of the American boot and shoe industry given on p. 290), a small rise in consuming power may do little to prevent a crisis of glut.

It may be, therefore, that the actual policies which they pursued in 1929 resulted in the capitalists getting the worst of both worlds; that these policies made production finally unprofitable without preventing glut. In essence, however, this is not a question of much substance. The essential point is that, whatever they did, the capitalists were bound to precipitate the crisis in one way or the other. For them it was in this case also merely a question of "the more or less rational treatment of the inevitable."

This, then, is the lesson which we cannot avoid drawing from the circumstances in which the crisis of 1929 occurred. We now turn to the question of recovery. Now how does the *Economist's* chart bear on the question of the recovery which has been perceptible since the summer of 1932? We see that from 1931

onwards the rise in real wages is stopped everywhere, except in France and America, and, in some cases, the lines turn downwards. Here are the *Economist's* comments :

"The year 1932 was a period of gradual readjustment of labour costs, shown in the decline of real wages in Japan, Germany, the United States, and the United Kingdom and, as was pointed out in a series of articles on relative prices in the *Economist* of May 1933, the stage was set for a revival in the spring of 1933. In the United Kingdom and in Japan readjustment was achieved by currency depreciation. Germany, and for a time the United States, chose the more painful method of reductions in money wages. An example is the German emergency decrees, under which all official wage rates were reduced by 10 per cent in January 1932. France was less successful, for in that country real wages continued to rise in 1932 and in 1933."

There seems little doubt that, just as a rise in real wages proved to be the harbinger of the crisis, so the recovery (such as it is) has been primarily effected by an arrest of this rise. (At the cost of repetition let us repeat that even an arrest of a rise in real wages necessitates in contemporary conditions a reduction in money wages. Prices, gold prices, that is to say, are perpetually dropping because of the fall of  $\pounds$ —because of rationalization in the broadest sense of the word. A level line in the chart conceals a steady drop in money wages. Or, of course, it may conceal constant money wages and a steady inflation of paper prices after a departure from the gold standard.) France and America, however, seem to be exceptions to this rule. In the case of America, we have already seen that there is the gravest doubt whether, in the peculiar conditions of the N.R.A., a trend based solely on hourly wage rates, has any relevance to the real earnings of the population at all. We have seen that, even according to the leading official of the New Deal, American real wages have now begun to fall. The degree of recovery achieved, moreover, has been very moderate. (Mr. Richberg's figures have been widely criticized as presenting a quite unjustifiably favourable picture of the workers' real

position under the New Deal. We shall, however, accept them, for even as they stand they serve to support our thesis.) In the case of France, the simple fact is that, just as there has been no adequate arrest of the rise in real wages, there has been, also, no recovery. There the slump is still unmitigated.

Thus both the downswing and the upswing of the present cycle illustrate the truth of Marx's analysis; and they expose the inadequacy of the under-consumptionist analysis. If it was true that all that was wrong with capitalism was that it did not pay high enough wages to enable the commodities which it produced to be sold, then we must have found that the closing stages of the boom and the downswing of the slump were characterized by a fall in real wages, or at least by a failure of real wages to rise. But we have seen that it was just at this time that real wages were rising. Similarly, if the under-consumptionists were right we should expect to find that recovery was inevitably associated with a rise in real wages. But it was not until the spring of 1933, when real wages were drastically reduced, that recovery began. And in "less successful" countries, as the *Economist* calls them, like France, where "real wages continued to rise," recovery has failed to put in an appearance at all.

These recent facts cannot fail to demonstrate to us that the under-consumptionists of all kinds have at best got hold of only one half of the truth about the cause of capitalist crises. It is quite true that the basic reason why capitalism is in permanent difficulties is because it increasingly fails to distribute enough purchasing power by way of wages, etc., to the mass of the population to enable them to buy the consumers' commodities which the system produces. But it is quite false to deduce from this that a ready remedy would be provided if capitalism distributed some more purchasing power; if wages were raised and social services increased, that is to say. For if that were done, first accumulation and then production itself would become increasingly unprofitable, and would soon, therefore, have to cease. Moreover, it turns out that the proximate cause of the present or "great" depression may not have been so much a failure to distribute enough purchasing power to make possible the sale of the commodities produced, but a tendency



to distribute too much purchasing power to allow of production being profitable.

Capitalism is continually menaced by the Scylla of its periodic inability to sell its products, and by the Charybdis of a collapse of the profitability of production. The under-consumptionists see the rock but ignore the whirlpool.

It remains to apply the Marxist analysis to the present recovery and to form an estimate of the extent and duration of the upward movement. It is clear that, unless there is no validity whatever in the analysis which alone enabled its adherents to predict the slump, a revival so produced can have but one ending. Once again capitalism is overcoming one barrier (and overcoming it but very partially) by placing the same barrier, but now heightened, a little further along the road which the system must travel. The rate of profit, briefly revived by the slaughtering of the values of constant capital, by the carefully organized destruction of commodities, by a serious diminution of the rate of production over a period of years, and, above all, by the raising of the rate of surplus value by means of drastic reductions in real wages, will once again be attacked by its old enemies. The magnitude of  $\bar{y}$  will begin again (indeed, it has never ceased) to fall, and to fall ever more precipitously. As the demand for labour power increases, it will become less easy to drive down money rates of wages and to slash social services. A tendency for real wages to rise, due to the ever accelerating fall in prices, will once again make itself felt. But, though this rise will be sufficient to check accumulation, it will certainly not be sufficient to allow of the absorption of the great mass of consumers' goods which will then be coming on to the market. The revival will collapse.

#### SUMMARY OF CHAPTER XXI

Exclusion of important elements of Marx's analysis from these pages; *viz.*, the question of disproportions between the departments of production and of the concentration of capital. This exclusion only to be excused if the great importance of Marx's crisis analysis is admitted.

What symptoms should we expect to find before the outbreak of a crisis if Marx is right? How do the facts of the great depression tally with what we might expect? The *Economist's* chart of real wages. Limitations of the statistics on which the chart is based. The apparent exception of American wages. The *Economist* attributes the slump to a decline in profitability due to rising real wages. We attribute it, however, to the appearance of the basic dilemma of capitalism in a particularly acute form. Some speculations as to which horn of the dilemma actually impaled capitalism in 1929. An explanation of the apparent difficulty that British real wages rose in spite of the persistence of unemployment. The rise of American real wages: causes. The myth of Fordism. Its widespread acceptance. The Marxist spokesman alone keep their heads.

The *Economist's* chart and the recovery. The slashing of real wages in 1932. The failure of the French capitalists to cut real wages. "The less successful countries."

The under-consumptionists see only half the truth. It is true that capitalism does not distribute enough purchasing power. But this does not mean that a ready remedy is for it to distribute some more. For, if it did, production would at once become unprofitable. The under-consumptionists see the rock, but ignore the whirlpool.

If we apply the same analysis to the recovery we must be convinced of its impermanence.

## CHAPTER XXII

### *Fascism : Social Democracy and Capitalist Crisis*

THE enormous bubble of American prosperity has been pricked ; semi-chronic crisis is now writ large over the face of the earth. In such circumstances, it might have been supposed, no further mistakes as to the real nature of capitalism were possible. In particular, it might have been supposed that the myth of the possibility of a harmonious, stable capitalism, which had solved all its difficulties by paying high wages, had been finally exposed. This is by no means the case.

Indeed, it will be found that an understanding of the present economic situation of the capitalist world, and of its possibilities and its impossibilities, is still never achieved if the observer has not grasped that "innermost essence" of capitalism which Marx laid bare in Volume III of *Capital*. The Great Depression has not taught non-Marxist observers anything as to the nature or the cause of capitalist crises, and hence of the possibility or impossibility of their avoidance.

We need not say anything of the less responsible capitalist economists, the cells of American Brains Trust, or of the ordinary run of Lib.-Lab. optimists in Britain. These ladies and gentlemen are now prating of a new period of prolonged capitalist revival. The more serious of their own colleagues, such as Professor Robbins, are competent to instruct them, if indeed they are capable of instruction. It is a more important matter, however, when a writer with the widespread influence in the British socialist movement of Mr. G. D. H. Cole reveals that he has not comprehended the nature of the situation. It will be well worth while to examine Mr. Cole's views on the contemporary situation not only for their own importance, but because they are almost perfectly typical of the views of a distinct and substantial strata of opinion, which exist both in Great Britain, and, in a slightly different form, in the United States. Mr. Cole has recently published a book with the challenging title of *What Karl Marx Really Meant*. In the second chapter he has a section entitled "The Contradictions of Capitalism." In it he

recognizes that the whole world to-day is a fulfilment of Marx's predictions. "It is undeniable," he writes,

"that, in this matter of the inherent contradictions of capitalist economy, the present situation of Capitalism fully bears out all the essentials of the Marxian analysis. A generation ago, it was common to laugh Marx's predictions to scorn, and to point, in refutation of them, to the advancing standard of life which Capitalism was able to offer to the workers in all the advanced countries. But no one can dismiss Marx's contentions in this facile fashion to-day. World Capitalism does stand convicted of a lamentable failure to make use of the rapidly increasing productivity which the progress of knowledge and invention has put within men's power; and world unemployment and the cry about 'over-production' are sufficient witnesses to its failure." (*What Karl Marx Really Meant*, chap. ii, p. 64.)

Unfortunately, however, the rest of the section does little to assure us that Mr. Cole has understood why it is that Marx's predictions have come true so far, or why they should continue to come true in future. For Mr. Cole's argument reveals that he believes, and what is more ascribes this view to Marx, that the essential contradiction of capitalism is that international competition prevents the capitalists of any given state from raising the real wages of their workers sufficiently to enable these workers to buy all the consumable products of industry.

It follows from this view that it *would* be possible for the capitalists of any given state to pay wages sufficiently high to effect this purpose if they could "insulate" themselves from the effects of international competition. Mr. Cole believes that for capitalist countries with sufficient natural resources this is perfectly possible.

"A country which has so wide a diversity of natural resources and so large a population that it can produce, without serious economic sacrifice, nearly everything it needs for an advancing standard of life is in a position, by adopting Economic Nationalism, to escape the fatal barrier to a high-wage policy

which international competition sets up." (*What Karl Marx Really Meant*, chap. ii, p. 61.)

He believes that the United States of America is a capitalist country in this happy position. And he believes that this is just the policy which Mr. Roosevelt is trying to implement. America, he writes, is

"heading uncertainly towards an experiment in controlled capitalism on a basis of Economic Nationalism, and with a deliberate endeavour to apply a high-wage policy as a necessary element in its success."<sup>1</sup> (*What Karl Marx Really Meant*, chap. ii, p. 61.)

It is clear from these passages that Mr. Cole supposes that there is nothing which makes it impossible for a sufficiently strong and wise government of a sufficiently self-contained capitalist state to make the system work in perpetuity without crises. All that such a government need do is to force the capitalists to pay wages sufficiently high to enable the masses to buy all the products of industry. There is nothing, for example, to prevent the New Deal succeeding if Mr. Roosevelt is able to force up the rate of wages and avoid being pulled off his course by vested interests.

It is hardly necessary to remind the reader that nothing could be more flatly at variance with Marx's argument than this conclusion. If all Marx's intricate and subtle chapters on the unravelling of the inner contradictions of capitalism had meant was this, then Mr. Cole would indeed have effected a much needed simplification ! Marx, however, as we have seen in detail, meant almost exactly the opposite of this. As a reading of even the quotations from *Capital* contained in the preceding chapters of this book will show, Marx considered that high wages, that indeed any tendency for wages to rise above their value, was the most fatal thing which could possibly happen to capitalism. He believed that such a tendency would immediately make the system unworkable by reducing the rate of surplus value, and so

<sup>1</sup> As an example of how general is this view amongst intellectuals holding liberal opinions, we may instance Mr. H. G. Wells' enunciation of it in his recent (1934) conversation with Stalin.

administering the *coup de grâce* to the rate of profit. It was necessary to the proper functioning of capitalism to hold real wages down to their value (*i.e.*, subsistence level). The best way in which recovery from a crisis could be effected was to force wages, temporarily, even below this level.

In a volume which sets out to tell us what Karl Marx really meant, this error of fact is serious. Moreover, as we have shown above, the view that high wages are positively a specific for producing crisis; that the lowest possible, instead of the highest possible, wages are the one way in which the capitalists can, in modern conditions, hope even to postpone crises, or to secure temporary recovery from them, is not only Marx's view. It is a view which is endorsed by all the serious thinkers amongst capitalist economists. It is a view which capitalist leaders have always acted upon as a result of their accumulated experience. And it is a view the validity of which has been proved to the hilt by the events of the last ten years all over the world.

Mr. Cole has fallen into this extraordinary error by neglecting the main factor of the situation, the falling tendency of the rate of profit. He, like so many others, has observed only one horn of the capitalist dilemma. He has seen, and in this, of course, he is quite right, that the holding down of real wages to the subsistence level must in the end produce a crisis by making it more and more difficult to realize by sale the surplus value which these same low wages have enabled the capitalists to extract. But he has failed to see that high wages would be still worse for the system, for they would make it impossible for the capitalists even to extract surplus value (on a sufficient scale), let alone to realize it.

Mrs. Barbara Wootton in her *Plan or No Plan?* has shown (pp. 124-5) how one school of capitalist economists sees one horn of this fundamental dilemma and one the other, but that neither sees both. What she well describes as that "whole body of such left wing liberal and right wing socialist opinion as dabbles in economic theories at all" believes, having had their eyes opened for them by Mr. J. A. Hobson, that "the capitalist system collapses because it invests too much." (In our terminology this school says that if the capitalists maximize accumulation, they will minimize consumption, and so provoke crisis

from their inability to sell.) On the other hand, "influential economists" (the Hayek-Robbins school) proclaim, she writes, that "Capitalism collapses because it does not invest enough." (This school sees that unless accumulation is maximized the amount of profit will begin to diminish, production will immediately decrease, and a crisis be provoked.)

Mrs. Wootton says of these two contradictory schools of capitalist thought that "they cannot both be right." On the contrary, as far as their negative case goes, they are both perfectly right. For what is here in question is the basic contradiction of capitalism. The system runs into a crisis one way if it maximizes accumulation and another way if it maximizes consumption. By the same line of argument, however, both schools can be shown to be wrong on their positive sides. For each proposes a remedy, which, while it enables the system to avoid one horn of the dilemma, infallibly impales it upon the other. Thus each school is able to show, and does show, that the other's constructive proposals are no remedy, that they are, indeed, worse than the disease.

Mrs. Wootton is right, however, in instinctively preferring the Hayek-Robbins orthodox school to the Lib.-Lab. under-consumptionists, as enunciating sounder capitalist doctrine. For this school has only become wrong with the completion of capitalism's "task and privilege," namely, the development to a certain point of man's productive powers. Until that task was accomplished, it was true that it was possible to maintain the profitability of production and thus to keep the system going, by maximizing accumulation and minimizing consumption. It was not, at that time, insane to utilize all increments of wealth for the purpose of creating further increments of wealth. An acceleration of accumulation sufficient to offset the fall in the rate of profit was attainable. Fresh fields and pastures new were always being opened up in which capitalism could begin its task all over again.

Mr. Cole is still under the spell of the high wages doctrine of the nineteen-twenties. As Mrs. Wootton points out, he is at bottom a follower of Mr. J. A. Hobson's under-consumptionist theories. Nor, unfortunately, is this error of economic theory without important political corollaries. Mr. Cole proceeds

immediately to apply his theory of the economic practicability of a high wage capitalism, if only this policy can be politically enforced upon the capitalists, to the contemporary political scene. He tells us that any attempt to impose "a policy of high wages, designed to enable capitalism to escape from its inherent tendency to a failure to employ the resources of production to the full," involves "a completely centralised control of all the vital factors in the economic system." It involves, Mr. Cole proceeds, "either Fascism or Socialism." He considers first the economic problems and prospects of a fascist central authority. "If," he writes,

"the end is naked capitalist autocracy rather than Socialism, what will happen next? Will the capitalist autocrats be able so to overcome their instinctive opposition to working-class claims as, even after they have destroyed for their own security the independent organisations of the working class, to persist in handing over to the defeated workers the higher and higher incomes required to afford an adequate outlet for the expanding product of industry? If they do not, the old capitalist contradiction will recur, with a renewal of unemployment and business losses and stagnation, and a consequent re-emergence of the forces of discontent, to threaten and in the end to cast down their autocracy." (*What Karl Marx Really Meant*, by G. D. H. Cole, chap. ii, p. 63.)

This passage begins to reveal to us the view of fascism and its economic possibilities which Mr. Cole's error in economic thought involves. If the fascists do not pay high wages, Mr. Cole tells us, then crises will recur and fascism will break down. Does Mr. Cole imply, then, that if the fascists are wise enough to pay high wages, crises will not recur and fascism will succeed in creating a stable, permanent, and prosperous capitalist economy? Certainly this is only an implication latent in the above passage and it would be unfair to conclude from it alone that this was Mr. Cole's view of fascism. Unfortunately, however, Mr. Cole's view is made explicit in his concluding chapter. We find that Mr. Cole supposes that fascism is not merely a change in the methods by which the existing ruling class exercises its rule. On the



contrary, he believes that successful fascism represents the capture of power by an intermediate class of *petit bourgeois* standing between the capitalists and the workers and "profiting by their dissensions." This *petit bourgeois* class, Mr. Cole writes, reacts to the decay of capitalism by "becoming determined to defend it" (capitalism) "at all costs against the exponents of equality, by reconstructing it on a basis which will subordinate the conduct of large scale industry and finance to their claims." The emergence of this new class renders obsolete, Mr. Cole writes, "Marx's analysis of the class struggle fought out between the workers and the capitalists" (p. 245). Nor is there anything inherently impossible, Mr. Cole believes, in the fascist *petit bourgeoisie* successfully reconstructing capitalism and "subordinating it to their claims."

"Doubtless, they can hope to do this<sup>1</sup> only if they are in a position to reconstruct Capitalism, or to construct a new type of Capitalism, upon a basis consistent with the further development of the powers of production. But it is illegitimate to exclude out of hand the possibility of this being done." (*What Karl Marx Really Meant*, chap. ix, p. 295.)

How, then, we enquire, is the *petit bourgeoisie* to construct a new capitalism "consistent with the further development of the powers of production"? By two methods, Mr. Cole answers. By insulating their state from the effects of world competition and then by enforcing the "compliance of the great capitalists in a higher standard of living"—in a word, by implementing the policy of high wages. But it is, precisely, "illegitimate" *not* "to exclude out of hand the possibility of this being done." There is nothing more certain under heaven or on earth than that any attempt at intensive economic nationalism combined with high wages would immediately send the rate of profit to zero and so stop all capitalist production whatsoever. Not to have understood this fact reveals a basic incomprehension of the very nature of capitalism.

Nor can we prevent ourselves from observing that Mr. Cole's doctrine of economic nationalism combined with high wages is

<sup>1</sup> "to do this"—to seize and hold power, as the context makes clear.

precisely the doctrine preached by fascist parties. Mosley in Britain, Hitler in Germany, and all the rest of them, with varying degrees of clarity, have advocated this policy. We have reached the uncomfortable conclusion, then, that Mr. Cole sees no grounds for disagreement with the fascist economic programme. What, then, is his objection to fascism? If it were possible to build up a new and reformed type of capitalism, self-contained, stable, able to use our productive resources to the full, and capable of giving the workers a higher standard of living, would there not be a very great deal to be said for doing so? And, indeed, Mr. Cole goes on to make it clear that his objection to fascism is an objection to its methods, not to the aims which, he supposes, the *petit bourgeois* fascists are striving for.

Revolutionary writers are often accused of calling everybody a fascist who does not agree with them in all particulars. It must not be thought that we are alleging that Mr. Cole has fascist leanings. Fascist methods and ideology are unquestionably far too repugnant to him for that. But it is impossible not to cite the passage in which Mr. Cole himself expressly states that the form of economy, the reconstructed and reformed semi-capitalism, which he and his friends of the British Labour Party are striving for, is of the same character as the economic system held out by the fascists as their goal. Mr. Cole is discussing the prospects before the various countries of the world. Russia has been won by the workers. Germany and Italy have been captured by the *petit bourgeois* fascists. The United States will probably go along the same fascist road. And then Mr. Cole comes to Great Britain.

“ Finally, Great Britain may succeed in establishing a form of parliamentary Socialism which will leave large elements of Capitalism still in operation, and be distinguished from the systems dominated by the *petit bourgeoisie* less in its mechanism than in the nature of the forces which are in control.”  
(*What Karl Marx Really Meant*, chap. ix, p. 301.)

The more we reflect upon this passage the graver its implications become. It is written, we must remember, by the most

prominent and influential theorist of the left wing of the British Labour Party. It should be read and re-read by those millions of sincere men and women within the Labour Party who believe that one more attempt to achieve socialism by means of "a revolutionary Parliamentary majority" should be made. Can we possibly avoid the conclusion that Mr. Cole here defines the task which he and the other leaders of the left wing of the Labour Party would undertake if they came to power, as the establishment of the same type of "mechanism," the same type of economic system, that is, as the *petit bourgeois* fascists are supposed to establish? Mr. Cole has already told us what that "mechanism" consists in. It consists in a strong central control which will, without expropriating the capitalists, insulate the economic system from foreign competition and then impose a high wage policy upon the capitalists.

Now we are not suggesting that there is anything to be shocked at in the fact that Mr. Cole and the left wing of the British Labour Party are aiming at the same objective as the fascists. (Or, rather, at the professed objective of the fascist leaders and the illusionary objective of the fascist rank and file.) If the objective is a sound one, it is no worse because the fascists think that they are attempting to get there. The tragedy is, on the contrary, that both Mr. Cole and the Parliamentary socialists, and the rank and file fascists, are, as we have shown, striving for an inherently impossible thing. Because none of them have understood the essential nature of capitalism, they are aiming at something which is, from the very nature of reality, impossible of attainment.

Here, perhaps, we have the most signal example of the dreadful consequences for practice of insufficient and incomplete economic theory. Mr. Cole is very influential. He and the other leaders of the left wing of British Labour, such as Sir Stafford Cripps, Mr. Pritt, Mr. Mellor, and other leaders of the Socialist League, are able to prevent a large number of British socialists from taking the revolutionary path. Mr. Cole has now defined the objective of this whole school of thought. It is, to put it shortly, a corporate state, controlled, not by the fascists, but by Parliamentary socialists, and evolving, it is no doubt believed, from a

controlled capitalism towards socialism.<sup>1</sup> It is an attractive and plausible programme, *for those who have not understood the nature of capitalism*. And yet it leads straight to division and defeat, for it diverts vital elements of the working class forces from the real struggle with the ruling class. It utterly wastes their efforts upon attempting an inherently impossible task. Moreover, it has even more serious consequences. Since it endorses the fascist claim that it is perfectly possible to solve the crisis by economic nationalism combined with the imposition of high wages, without the expropriation of the capitalists, it provides but the flimsiest of objections to the fascist case. For many workers will conclude that if even the socialists admit that it is "illegitimate to conclude" that the fascists cannot solve the crisis, there is a great deal to be said for supporting the fascists. After all, the fascists can, and visibly do, secure the support and endorsement of the largest capitalists, and this the Parliamentary socialists can never hope for. The fascists have unquestionably a far easier road to power. If, then, on Mr. Cole's own admission, both the Parliamentary socialists and the fascists are out to set up the same economic "mechanism," the same form of economic system, that is to say, why not support the fascists?

There is no answer to this simple argument. If it were true, as Mr. Cole believes it to be, that the fascists are the agents of a separate class, opposed to the great capitalists, and able to set up a workable economic system, which could end the present chronic state of crisis and inaugurate, as he writes, "a whole new phase of social development, based on a system of state-controlled capitalism under *petit bourgeois* influence," then there would be a great deal to be said for the fascists. It is, at the very least, far from clear why the workers should prefer Mr. Cole and his friends who, it turns out, are only trying to do the same thing with far less chance of obtaining political power.

This whole conception of the fascists as an independent class force based upon the *petit bourgeois* is, however, totally false. It

<sup>1</sup> The Socialist League's leaders have in recent statements made it clear that they realize that the official objective of the Labour Party has become a version of the corporate state and that they object to this. But, hitherto, at any rate, their own statement of objectives has been in fact merely another version of the corporate state expressed in more militant language. Let us hope that they will see the necessity of changing this if they are to continue to criticize the official policy.

is, we see, bound up with the economic delusion that a high wage, insulated, controlled capitalism is possible. For it is true that this is at bottom the delusion of those sections of the *petit bourgeoisie* which do, undoubtedly, form the majority of the rank and file of fascist movements. Captain Rochm's Storm Troopers did undoubtedly believe, like Mr. Cole, that they were part of a mighty and revolutionary movement which was going to remodel the economic system so that it served their needs rather than those of Herr Thyssen and the great German capitalists. The illusion that such a remodelled, high wage paying capitalism is a possibility is, in the last analysis, the psychological basis of the mass support which fascist movements have sometimes secured.

It is extraordinary that it is still necessary in 1934 to refute the view that the fascist movements of Germany or of Italy were ever controlled by the *petit bourgeoisie* of those countries (which did largely compose them), or that they have served the interests of this intermediate class. Have these movements attempted to construct a new type of capitalism, paying high wages, and thus enabled to dispose of its products without glut or crisis? It is easy to put the matter to the test of experience. Have fascists movements when in power enforced, or have they attempted to enforce, a policy of high wages on the capitalists? Let us examine the course of wages in Italy and in Germany since the fascists gained power in those two states. For the course of wages in fascist countries will surely provide almost conclusive evidence of the nature of fascism.

The course of wages in Italy since the assumption of power by Mussolini in 1924 is not easy to follow since Italian economic statistics are notoriously incomplete. It is best, in order to avoid a controversy as to the facts, to rely wholly upon official figures. These show that even before the outbreak of the 1929 crisis, money wages were falling fast in Italy.<sup>1</sup> For instance, Signor Biagi, Secretary of the National Confederation of Fascist Syndicates, writing in the *Corriera della Sera* on March 26th, 1932, says :

<sup>1</sup> The reader will recollect that the *Economist's* chart presented in the last chapter showed that Italy was the one important country in the world in which real wages did not rise in the latter stages of the boom and early stages of the slump.

"Between June 1927 and December 1928, wages fell by about 20 per cent as a result of agreements between masters and men in connection with the stabilization of the lira. A further drop of approximately 10 per cent took place in 1929, and in November 1930 there was a general downward movement, in some cases not exceeding 18 per cent, but in particular instances involving as much as 25 per cent. Moreover we must not overlook the fact that many other adjustments were made in 1931."

After this little prelude of three successive and cumulative wage cuts of 20 per cent, 10 per cent, and then 18 to 25 per cent, the world economic crisis broke out.<sup>1</sup> The British Department of Overseas Trade's Report on *Economic Conditions in Italy 1933* is the best authority for what happened then.

"While the cost of living with an index figure of 93·78 in 1927 has fallen in 1932 to 78·05, a difference of 15·73 per cent, industrial wages have been reduced by much larger proportions. . . .

"Cuts have been made ranging from 16 to 18 per cent in the sheltered printing and woodworking trades, 25 per cent in the metal and chemical industries, to 40 per cent in the cotton industry. . . .

"To the above must be added arbitrary reductions effected by various means without negotiation, such as the re-grading of work-staff and the systematic reduction of piece-work rates."

The *Report* gives the following particular examples of wage cuts in individual industries :

	Per cent.		Per cent.
Chemicals . . .	.20-25	Silk Weaving . . .	. 88
Rayon . . . . .	. 20	Jute . . . . .	. 30
Rayon (Turin) . . .	. 88	Metal Trades . . .	. 23
Glass . . . . .	.30-40	Building . . . . .	. 30
Cotton . . . . .	. 40	Mining . . . . .	. 30
Wool . . . . .	. 27		

<sup>1</sup> In other words, the Robbins-Hayek policy was given a full trial in Italy and failed even to mitigate the severity of the crisis.

Since the appearance of this *Report* a Government order has appeared (April 1934) decreeing wage cuts of all Government employees, except the lowest paid, of between 8 and 12 per cent, and at the time of writing (September 1934) it is reported that Signor Mussolini is seeking the collaboration of Social Democratic leaders with a view to extending this new wage cut throughout industry.<sup>1</sup>

Mr. Paul Einzig, a warm friend of Italian fascism, sums up the position in Italy as follows :

"The amount of unemployment insurance is moderate, even for the low standard of living prevailing, and it is paid only for a short period. . . . In no country is it so easy as in Italy to obtain the consent of employees to a reduction in wages."

These quotations are from Mr. Einzig's book entitled *Economic Foundations of Fascism*. The title is just. The economic foundations of fascism are minimal unemployment insurance benefit and extreme ease in reducing wages.

The course of wages in Germany since the assumption of power by Hitler in January 1933 is even more difficult to estimate exactly. Once again it will be well to rely upon Nazi official figures.

A comprehensive survey of the German wages situation, which based itself exclusively upon official figures, appeared in the *Economist* for November 10th, 1934. That journal's Berlin Correspondent, writing from Berlin on November 7th, headed his article "The Decline in Real Wages," and began it as follows : "The serious rise in the cost of living became acute last week, and compelled the Government to take measures to propitiate consumers." "According to the last official return," he continues, "which is long out of date, nominal wages have declined

<sup>1</sup> This cut has now been enforced. On December 4th, 1934, the British Press announces a wage cut of 10½ per cent for 75 per cent of Italy's industrial workers. On this date just under one million of Italy's some 4 million insurable workers were totally unemployed. The best epitaph on Italian fascism certainly remains Mussolini's remark to the Senate on December 18th, 1930 : "Fortunately the Italian people is not yet accustomed to eat several times a day. Its standard of living is so low that it feels scarcity and suffering less." (*Corriere della Sera*, December 19th, 1930.)

by about 1 per cent since the Nazis attained office. But the nominal wage returned is the average wage fixed by collective agreement. In the past two years the average nominal earned wage has fallen, at least in many important branches, owing to 'stretching out' of limited work, and to compulsory reductions of working hours. Hence the effective real earned wage has fallen much more than would appear on a mere basis of the small decline in collective agreement wages and of the rise in the cost-of-living index.

"According to the old Reich index the cost of living rose from 116.6 in April, 1933, to 122.5 in September, 1934; the new index, as revised retrospectively, shows a rise from 115.9 in April, 1933, to 121.6 in September, 1934, and 122.0 in October, 1934. Ever since 1925, when it was first compiled, the old index was criticised as misleading, as underestimating, in times of rising prices, the advance in the cost of living. Though the weighting of the new index differs in some respects considerably from those of the old, the results do not materially differ. It is certain that neither expresses the recent movement. This is particularly true in the case of all those families which, owing to the official unemployment measures, are not earning the full standard wage. Foodstuffs, which for this class are of the utmost importance, such as potatoes, some fats, and vegetables, have lately risen enormously in price; in some cases by 200-300 per cent."

Thus, according to official figures, money wages had fallen 1 per cent and cost of living had risen about 6 per cent between April 1933 and September 1934. Thus real wage rates had fallen about 7 per cent. To this must be added first the above mentioned increase of short time working and "stretching out," second the "serious rise" in the cost of living which only began in the first week of November 1934, and is not, therefore, shown in these figures, and, third, the fact that the prices of bare essentials such as "potatoes, some fats, and vegetables" have risen as much as 200-300 per cent.

On the whole, therefore, while it would be an exaggeration to say that Herr Hitler had yet achieved anything approaching the prodigies of wage cutting achieved by Signor Mussolini, yet his efforts in that direction are undeniable, and are, at the time



of writing (November 1934) just beginning to bear substantial fruit.

Do these facts suggest to us that Italian or German fascism are *petit bourgeois* movements intent to enforce a policy of high wages on the capitalist class and so usher in "a whole new phase of social development"? They do not. The truth is that fascism is always and everywhere the instrument, not as Mr. Cole supposes of the *petit bourgeoisie* using the great capitalists as its unwilling allies, but of the great capitalists using the *petit bourgeoisie* as its dupes.

As I write these lines (July 3rd, 1934) the roll of drums which sounded at the executions of Roehm, of Heines, of Ernst, and some hundreds of other leaders of the Storm Troops, is echoing across Europe. Why have these murderers been murdered? They have been murdered because they or their followers were suspected of dreaming of that high wage paying, controlled capitalism, in the possibility of which Mr. Cole still believes. Why has the Brown Army of dupes been shattered? It has been shattered because the economic policy of Hitler's masters, of Thyssen, of Krupp, of Siemens and of the Junkers, must now perforce become even more flatly at variance with that dream of stable *petit bourgeois* security for which the Brown Army fought and ravaged.

The truth is that desperate measures for the purpose of restoring the rate of profit are being undertaken by the German ruling class, using Hitler as their executive instrument. *And they are the capitalistically correct measures.* Mr. Cole, with that curious belief of all Social Democratic theorists that he can teach the capitalists how to run their businesses, supposes that the German capitalists are committing a stupid blunder when they slash and slash again at wages and social services. But the German capitalists know very well what they are doing. They are restoring the rate of profit of German industry in the only way by which it can be restored. Nor have they been altogether unsuccessful. It would be idle to deny that there has been an increase in economic activity within Germany. The figures showing the profitability of German industry have moved between the fourth quarter of 1932 and the fourth quarter of 1933, as follows (*Financial Times*, September 17th, 1934):

	4th quarter	
	1933	1932
Number of companies considered . . . . .	920	922
Nominal share capital (mill. Rm.) . . . . .	7,492	7,662
Depreciations (mill. Rm.) . . . . .	572	510
Net profits (mill. Rm.) . . . . .	341	294
Number of companies showing net profit . . . . .	719	571
Net profits as per cent on share capital . . . . .	4.11	3.27
Net deficits (mill. Rm.) . . . . .	127	386
Net deficits as per cent of share capital . . . . .	1.53	4.44
Amount of dividends paid (mill. Rm.) . . . . .	259	240
Amount of dividends as per cent on share capital . . . . .	3.77	3.43

No one can accuse the German capitalists of suffering from illusions as to the real nature of their system. They do not need to have read the third volume of *Capital* to tell them that the only way to recovery lies through a restoration of the rate of profit at all costs and at all hazards. And the rate of profit can only be restored at the expense of the wages of the German workers.

This is not to deny that such wage cutting must in the end produce a new crisis by narrowing still further the market for the products of German industry. This is the horn of capitalism's dilemma which Mr. Cole and the under-consumptionists do see, and it is perfectly real. This is the nemesis which awaits even the "soundest" capitalist policy. This is the factor which must sooner or later result in an unprecedented new economic crisis in Germany.<sup>1</sup> It is probable, however, that Mr. Cole and all under-consumptionists under-estimate the possibilities of temporary capitalist revival which sufficiently ruthless wage cutting, a sufficiently violent reduction of all working-class standards, can effect. It is undeniably possible to create a momentary boom if the rate of profit can be sufficiently restored. Moreover, however transient a revival produced by these means may be,

<sup>1</sup> "The last cause," writes Marx, "of all real crises always remains the poverty and restricted consumption of the masses as compared to the tendency of capitalist production to develop the productive forces in such a way, that only the absolute power of consumption of the entire society would be their limit." (Vol. III, p. 508.) The last cause, yes. But if you try to eliminate the poverty of the masses by raising wages, you will get a first cause of crisis quickly enough in the collapse of the rate of profit and the consequent cessation of production.

these are the only possible means of obtaining any revival at all.<sup>1</sup> Accordingly, they are unquestionably the correct policy for every hard pressed capitalist class.

This consideration reveals to us the real nature and function of fascism. Far from being a *petit bourgeois* movement, trying to impose an impossible high wage policy on the great capitalists, it is a movement owned and controlled, bought and paid for, from start to finish by these great capitalists themselves. And its essential and indispensable function is to smash everything and anything which stands in the way of the reduction of wages to the lowest possible level. And this function the fascist leaders most faithfully perform. Every fascist party that has come to power has done three things. It has smashed (a) the trade unions, (b) the co-operatives, and (c) the working-class political parties. Does this policy seem a logical preliminary to an attempt to impose high wages on the great capitalists? It does not. Nor is it. It is the essential preliminary to an unheard of reduction in working-class incomes from all sources. The trade unions are smashed in order to put the workers at the mercy of their employers, so that any wage rates which the employer desires may be imposed upon them.<sup>2</sup> The co-operatives are smashed in order that the workers may have no power to undermine monopoly prices. The working-class political parties are smashed in order to make possible the wholesale revocation of social services.

The political function of fascism is to serve as the bludgeon of the greatest monopoly capitalists. The economic function of fascism is to raise, at any hazards, the rate of surplus value in order to offset the ever growing sag in the other determinant of the rate of profit. That these are the twin functions of fascism can be verified by observing the actions of every fascist party in power. And observation of what fascist parties actually do when they come to power can alone reveal to us what is the

<sup>1</sup> Wage cutting is the only substantial measure for the restoration of the rate of profit open without war to the German capitalists and to most others. Imperialist expansion, however, is still open to some others, *viz.*, the Japanese capitalists.

<sup>2</sup> "Our corporate organization will as its first work restore absolute leadership to the natural leader of a factory, that is, the employer, and will at the same time place full responsibility on him. Only the employer can decide." (Dr. Ley, Leader of German Labour Front, speaking on June 10th, 1933, on "Fundamental Ideas on Corporate Organization and the German Labour Front.")

The quotation is taken from *Fascist Germany Explains* by Celia Strachey and John Gustav Werner.

essential nature of fascism, when stripped of its enveloping mass of demagoguery, deceit and illusion.

#### SUMMARY OF CHAPTER XXII

The slump has not revealed the nature of capitalism to non-Marxist observers. Mr. G. D. H. Cole on the nature of capitalist contradictions. Mr. Cole thinks, and alleges that Marx thought, that the main contradiction of capitalism consists in the inability of the capitalists to pay high wages owing to international competition. He believes that any capitalist state which is large enough to be able to "insulate" itself *can* pay high enough wages to provide a market for all of its products. He believes that Mr. Roosevelt's New Deal is an attempt to set up such a controlled capitalist "autarchy."

Marx, however, in fact took an exactly opposite view. He considered that high wages were incompatible with the continued existence of capitalism. He has seen one horn of the fundamental dilemma of profits or plenty, but not the other. Mrs. Barbara Wootton shows how the policy of each school of capitalist economists avoids one horn, only to impale the system upon the other. Mr. Cole at heart an under-consumptionist. He applies his economic analysis to the contemporary situation. He believes that crisis will overtake the fascists if they do not pay high wages. He implies that they can prevent crisis if they do pay high wages.

Mr. Cole's general view of fascism. Fascism as the movement of the *petit bourgeoisie* as an independent social class. He considers it possible for the fascist *petit bourgeoisie* to establish a stable, high wage paying capitalism. This view involves a total misconception of the nature of capitalism. Mr. Cole shown to accept the fascist economic objective. The objective of the British parliamentary socialists defined as the attempt to set up the same type of controlled, high wage paying, capitalism as the fascist rank and file desire to set up. The objection to this objective is not that the fascists share it, but that it is inherently impossible of achievement.

Grave consequences of wasting the workers' energies on

attempting to achieve this inherently impossible objective. Serious effect upon the workers' minds of the acceptance of the fascist claim that it is possible for them to solve the crisis. If the parliamentary socialists and the fascists are on their own admission attempting to do the same thing, why not support the fascists who have certainly the better chance of being given power?

The conception of fascism as an independent *petit bourgeois* movement bound up with the illusion of the possibility of a stable high wage paying capitalism.

Has fascism in fact, represented an attempt to impose high wages on the capitalists?

The course of wages since the accession of the fascists (*a*) in Italy, (*b*) in Germany.

Fascism always and everywhere a movement owned and controlled by the great capitalists. Its essential economic function to restore the rate of profit by cutting wages. Relative soundness of this policy from a capitalist standpoint. The profitability of German industry partially restored by this method. The fact that such a policy must in the end produce a new crisis by destroying the internal market admitted. The twin functions of fascism, as shown by the deeds of every fascist government, are (*a*) to destroy all possibility of resistance to the will of the greatest monopoly capitalists, and (*b*) to restore the rate of profit by unprecedented wage reductions.

## CHAPTER XXIII

### *The Function of Theory and the Cause of War*

WE cannot, it is clear, understand fascism unless we understand the nature of capitalism and its crises. An incomprehension of the nature of capitalism alone makes it possible to believe that the fascists can solve the economic crisis ; and an acceptance of this possibility leads towards an acceptance of fascism itself.

We have discussed Mr. Cole's failure to understand at all what capitalism is and why it is breaking down. We have done so because Mr. Cole is a typical and influential spokesman of an exceedingly important school of thought. This school of thought, it is not too much to say, still dominates the organized activities of the British working class. Mr. Cole, it is true, speaks especially for the left wing of the Labour Party. But the dominant official leaders of that party, and of the British trade unions, differ from him in emphasis and in mode of expression alone. Upon the essential point they are in agreement. The whole of the present official leadership of the British workers looks forward, like Mr. Cole, to the possibility of an organized or planned, high wage paying, and centrally controlled capitalism. Some of them, like Mr. Cole, believe that such a system can be caused, under their fostering care, to evolve towards socialism. Others, like Mr. Morrison and Mr. Citrine (and in this they are comparatively realistic) put far more emphasis on the immediate phase of a capitalism organized from their future ministerial offices in Whitehall, or Smith's Square, and far less on any eventual evolution towards socialism. But that is the extent of the difference between the left and right wing leaders.

Nor is this the programme of all the leaders of the British Labour Party alone. It is the professed programme of all fascist parties, and the sincerely held ideal of the decent elements in the fascist rank and file. (This is the explanation of the sincere protestations of identity of aim and outlook which Nazi students, etc., often make to visiting members of the British Labour Party, to the latter's embarrassment.) Moreover, this dream of an organized, stable, high wage paying capitalism is the substance of the objective of many groups and parties,

besides the sections of the British Labour Party or of the fascist parties. It is the official policy of the American "Brains Trust" group, (surely the least profound body of thinkers to whom the destiny of a continent was ever entrusted?) In a suitable version, it is the programme of the American Socialist Party. It is the professed objective of all those "progressive" Conservatives and "modern-minded" Liberals (of all nations and of the League of Nations) who believe in what is called "planning"—and form everywhere little societies for the study of their plans.

Each of these diverse groups takes care, of course, to give this common objective an appropriate name. British Liberal and Conservative planners and American New Dealers, speak of a planned or organized capitalism. Official right wing Social Democrats would not care for such a phrase; they speak rather of step by step reforms without raising at all the question of what economic system it is which is to undergo these reforms. Left wing Parliamentary socialists describe, on the other hand, a transitional stage in the course of a rapid evolution towards socialism proper. Finally, the fascists have invented their own special term, namely, the corporate state. But it will be found on examination that these very different terminologies are all attempts to describe the same thing. All these parties, movements, or groupings are, in fact, holding out to us (with, in some cases, perfect sincerity) the possibility of establishing an economy which retains the essential principles of the present system, *viz.*, the private ownership of the predominant part of the means of production, their operation for profit, and the distribution of the products by means of exchanges mediated by a monetary circulation, but which eliminates the crises and convulsions, with their consequent miseries, which this system at present produces. All these groups believe that by various measures, by planning this or doing that, by reforming monetary policy there, or by imposing high wages here, it will be possible to eliminate what is bad in the existing system. Yet at the same time they believe that we shall be able to retain, at any rate for the present, those features of capitalism that they consider good, as well as those features the abolition of which would undeniably involve revolution. This is the underlying identity

of aim which is concealed by the very different language used by these different groups.

Nor is this aim any the worse for the number of diverse groups which subscribe to it. Unfortunately, however, as we have seen, whatever else may happen upon this uncertain planet, the establishment of a planned, stable, and high wage paying capitalism is impossible. Some of those who work for this objective do so in all good faith. But the men who hold the key positions of power and influence in the various parties which profess this general aim, know, as they reveal by their actions whenever and wherever they come to power, that quite other steps than those proposed by the planners are necessary if the private ownership of the means of production is to be maintained at all. So far as these responsible leaders are concerned, the achievement of a "reformed and planned" capitalism is merely the most acceptable and popular slogan by which support for a very different programme can be obtained. Indeed this slogan is so acceptable that it is not too much to say that one or other of the innumerable versions of a reformed economy, which yet retains the private ownership of the means of production and their operation for profit, is the professed objective of all parties and classes of persons in the world to-day, except two. The two categories of persons who show the one by their words and the other by their deeds that they do not believe in this vision are the revolutionaries organized round the Communist International, and those capitalist statesmen, bankers, and leading industrialists who actually bear the current responsibility for running the capitalist system.<sup>1</sup> These dissentient groups are but small. What are these amongst so many planners, it may well be asked? It is worth while to observe, however, that the revolutionaries and the responsible ruling groups of to-day are the two categories of persons who are compelled by their position in society to achieve a clear comprehension of the realities of the situation.

It is not difficult to understand the nearly universal character of the illusion of the possibility of a planned or reformed capitalism.

<sup>1</sup> To these must be added that select band of capitalist economists, such as Professor Robbins, Dr. Hayek, and some survivors of an older generation of professors, whose views we have so often had occasion to notice in these pages.



The first reflections of men or women, however intellectually gifted they may be, upon the nature of our present ills will almost certainly lead them to suppose that a cure is to be found in the control and planning of the existing system. For, to an extent seldom adequately realized, the mental pre-suppositions of a citizen of the western world are based upon an economy of private owners of the means of production, exchanging the products of their, and their workers', labours on the market. It is far more difficult (and it is far more rarely accomplished) than is usually supposed, for most people even to conceive of an economic system of any other kind. Moreover, it is, I think, not too much to say that it is impossible for anyone without serious economic study to understand why the existing economic system cannot be made to work. It seems self-evident to almost everyone that an exchange economy must work if only it is properly organized. People can understand easily enough that such a system may get, and clearly has got, out of adjustment and that it *may* break down entirely. But they cannot but suppose that it is at any rate possible to put it right. And if it is possible to put it right, is not this, they argue, the objective for which every sane man and woman should work? They cannot conceive at all what the Marxists can be talking about when they speak of "inherent contradictions" which make it flatly impossible for such a system to be planned or reformed. Most men and women assume (with Mrs. Wootton, for example) that the business of exchanging the products of their various activities to their mutual advantage is a fundamentally simple one. They cannot bring themselves to believe that it is really necessary to abandon the principle of profitable production and exchange and to undertake the unquestionably formidable task of organizing the whole of economic life afresh upon the new principle of purposive production for use.

We have attempted to exhibit in detail why this natural belief in the possibility of a reconstituted version of the present economic system is unfounded. It is based, as the reader will have apprehended, upon a failure to understand the uniquely and necessarily profit-making character of the present system; it is based upon a confusion between a system characterized by the production of use values as a means, merely, to the creation and

accumulation of exchange values<sup>1</sup> (in the form of surplus value or profit), and a system based on the direct and purposive creation of use values for their own sake. Each of these different types of system has its own possibilities, each is the economy which must inevitably exist at different particular stages in the development of man's productive power. But until the distinction between them is comprehended, the enquirer will inevitably fall into the error of supposing that we can have the advantages of both systems and the difficulties of neither.<sup>2</sup>

Nor, unfortunately, will the present day enquirer be assisted when he turns for guidance to those popular expositions and outlines of economics which are now so accessible. For the capitalist economists who have written them (not excluding those of them who hold socialist opinions) all have this major characteristic in common; they blur over this quintessential distinction. Nowhere and never in these often attractive volumes is the fact that capitalism can, and must, work for the purpose of accumulating profit, and for nothing else, placed in the centre of the picture. Consequently, it is never explained that the maintenance or restoration of the conditions in which profit can be made is the prerequisite of the very existence of this system, a prerequisite to which everything else must be sacrificed. And yet it is only if these facts are clearly exhibited that the picture presented by the world to-day becomes comprehensible. The contemporary popularizers have succeeded admirably in making economic theory simple and attractive; but unfortunately they have not at the same time been able to retain its significance. Hence the enquirer receives little of that assistance which might enable him to envisage the true nature of the problem. And yet such assistance is indispensable. It is almost impossible to gain by the unaided light of ratiocination an understanding of the essential nature of capitalism. It took the genius of Marx and Engels some twenty-five years of unremitting study to accomplish it. It is, as Marx said, "a very protracted work" merely to follow the trail which they blazed. Without this comprehension, however, we must remain blind and helpless in the

<sup>1</sup> "For the self-expansion of Capital," as Marx puts it.

<sup>2</sup> This major illusion is as old as Proudhon, the French Utopist of the eighteenth century. See Marx's *Poverty of Philosophy* for its exhaustive exposure.

dangerous chaos of our age. Without it we must sooner or later fall a prey to the kind of tragic illusion which has led the German people to their present fate.

It is indeed a characteristic tragedy of our time that everywhere millions of well-intentioned men and women are bereft of any but the most superficial intellectual discipline or tradition. As an inevitable consequence they spend their energies, and often give their lives, in the attempt to achieve what is inherently impossible. The results of their efforts are very different from what they expect. Sometimes their actions merely cancel themselves out, being self-contradictory. More often it is the inexpressibly tragic fate of these millions to become the dupes of men whose vision is clear, but whose aims are totally at variance with their own. To serve thus as the blind drudges of talented adventurers, who themselves are but the agents of the present ruling groups, is the fate which almost always overtakes those who fail to achieve an understanding of the nature of the contemporary world situation.<sup>1</sup> Moreover, this fate is shared, although in a less dramatic form, by those who retain the illusion of the possibility of reforming and replanning capitalism along the lines of democratic reform or parliamentary socialism. Though they do not pull the triumphal car of a Hitler or a Mussolini, they serve to drag into place and power the more soberly decorated vehicle of a MacDonald or a Roosevelt, or perhaps, in the future, of a Morrison. The masses who are held captive by the illusions fostered by parliamentary socialism or democratic reform are made to serve, that is to say, the same end as do the masses deluded by the blare and blast of fascism. They are both induced to hoist upon their backs political leaders who co-operate with (and in the last analysis always obey), each in their different ways, our real and unchanging rulers. These rulers compose the now comparatively small group of men and women who own the essential controlling blocks of the total capital of each national community.

A knowledge of the economic principles to which these pages have endeavoured to form some introduction can alone enable

<sup>1</sup> The most notorious of all these adventurers has himself said with startling frankness, "The German has not the slightest notion how a people must be misled if the adherence of the masses is sought." (*Mein Kampf*, first 11 editions.)

thinking men and women to escape from this humiliating disaster. Or, rather, such theoretical comprehension can alone enable them to escape from this fate without paying the frightful price of learning by experience. This is the price now being paid by the German people. There is already certain assurance that their bloody experience will enable them to find the only way out of their present agonies, namely, the expropriation of the German capitalist and landlord classes and the organization of planned production for use by a German workers' dictatorship. It is the function of theory, however, to minimize, at any rate, this well nigh intolerable price of experience.

These considerations enable us to reaffirm the claims that it is precisely to-day, in our time of violence and confusion, that a mastery of theory becomes, it is not too much to say, a matter of life and death for all of us. Economic theory in the deepest sense is an attempt to comprehend the nature of the existing economic system, and so indirectly to comprehend all that is built upon that system. In periods of tranquillity, when an existing economic system is functioning adequately, when its breakdown is not in question, the mastery of such theory may seem (though erroneously) unnecessary. It may seem possible to take (as modern equilibrium economics takes, for example) the existing system as an irreducible datum and to study only the deviations from that system's norms, but not the norms themselves. In our formidable epoch, however, when one whole method of carrying on the social and economic life of man is becoming impossible; when it is imperative to resort to an alternative method if barbarism is not to overtake us, economic theory assumes an extreme importance. Thus, exactly contrary to the vulgar assumption, the importance of theory increases directly with the severity of the crisis and the necessity for action. Theory is the eye of practice; theory alone can prevent the decisive actions to which we shall all in any event be constrained, from becoming self-contradictory. Without theory we can blindly do, but cannot prevent what we do from becoming the violent and purposeless deeds of a nightmare.

We have advanced high claims for economic theory. What then will the body of theory as to the nature of capitalism and

its crises, which has been briefly presented in this book, enable us to see our way to do ? It will not, it is true, enable us to set an exact date to capitalism, and so to the agonies which that system is now imposing upon the human race. It is interesting to notice, however, the powers of prediction which a perfect mastery of Marxian theory gave to Frederick Engels.<sup>1</sup> In a letter to Liebknecht on February 23rd, 1888, Engels writes that he thinks that the coming European war " will be a war of positions with varied success on the French frontier, a war of attack leading to the capture of the Polish fortresses on the Russian frontier, and a revolution in Petersburg, which will at once make the gentlemen who are conducting the war see everything in an entirely different light."

This prediction of Engels' shows also what Marxist theory does *not* claim to be able to predict. Engels never pretended to be able to say just when the war which he knew to be inevitable would come. (Indeed, I fancy that he personally expected it before 1914.) Moreover, the fact that he was able to predict so much of the character of the actual fighting was no doubt in

<sup>1</sup> If the reader requires a more modern instance, he should consult R. P. Dutt's notes in the *Labour Monthly* for February and March 1925, entitled respectively "The Restoration of Europe" and "The Gold Standard." In his new book, *Fascism and Social Revolution*, Dutt has a footnote of legitimate satisfaction in which he says of these 1925 notes :

" It was predicted that, as soon as the flow of new loans and credits (from America to Europe) should begin to dry up, and be exceeded by the necessary return movement of interest and amortization, requiring an enormous expansion of European exports in the overcrowded world market, this would necessarily precipitate a new crisis, leading to the shattering of the gold standard. To-day this analysis, made in 1925, and fully realized six years later, provides an instructive comparison of the effectiveness of the Marxist line in contrast to the complacent contemporary statements during that period of all the leaders and professional experts of capitalism on the success of stabilization and of the return to the gold standard " (p. 30).

Of course you may now find this piece of analysis in any work of popular capitalist economics—from Sir Arthur Salter's *Recovery* onwards. The difference between Dutt and Salter is that Dutt knew that all this must be going to happen, while Salter, after denying that anything of the sort could ever happen, describes it all after it has happened.

(See also the various pronouncements of the Communist International during the nineteen-twenties, especially the thesis adopted by the Sixth World Congress in 1928, and issued as a pamphlet entitled "Communism and the International Situation" [Modern Books Ltd., London].)

<sup>2</sup> R. P. Dutt's important pamphlet, *Marxism After Fifty Years* (published by the *Labour Monthly*, 7, John Street, London, W.C.1.), from which I take this quotation, should be consulted for evidence that this was not simply a lucky fluke, but an instance of Engels' insight into the general situation of world capitalism. (For this see also Engels' note on the future of crises on p. 574 of Vol. III of *Capital*.)

the nature of a brilliantly informed guess, made by a life-long *student of military affairs*. The essential points which Marxism enabled him to predict with confident certainty were that a great war between the rival imperialisms was coming and that it would be somewhere, and probably in Russia, interrupted by a workers' revolution. In the same way a comprehension of the nature of capitalism and its crises will not to-day enable us to say when or where the next inter-imperialist war will break out, and we shall be skilful indeed if we guess its character as well as Engels guessed the character of the last. But what such a comprehension does enable us to predict with certainty is that another imperialist war is coming, and that once again it will be interrupted, and this time in almost any of the great cities of the world, by a workers' revolution.

A knowledge of the economic principles which these pages have endeavoured to present will not only enable us to predict the coming of the next war. They will also, and this is more important, enable us to understand how and why war is the inevitable outcome of the economic and social relationships of the capitalist world. For it is not too much to say that, unless we understand the inner necessities of capitalism: that, unless we understand that there is an irresistible force within each capitalist economy, driving it towards expansion, we shall be unable to make any sense at all of what is happening in the world. Why is it that to-day every capitalist empire is rapidly, and at almost any risk to its financial stability, preparing for war? Why is it that already troops march and counter-march around the Central European frontiers: that by universal consent the world is back at a stage of "international tension" at least equal to that of the pre-war decade?

Even the most acute of non-Marxist observers are totally unable to answer these questions. It is clear that the outbreak of a new war would be the most perilous of all eventualities for the capitalist class of the world. Why, then, are our capitalist rulers visibly marching upon their fate? Non-Marxist observers are compelled to fall back on such strained hypotheses as that our rulers have "gone mad," or that mankind has innate "sadistic impulses" which periodically impel it to mutual slaughter, or (more usually) that, while their own capitalists, and those of

the states at the moment in alliance with them, are sensible and pacific, there unfortunately exist certain other states, often compared to "mad dogs," which are intent upon attack, and against whom, therefore, defensive wars must be waged.<sup>1</sup> At the present time, for example, the non-Marxist writers of the western democracies are unanimously agreed that, while Britain, France, and America are sensible and pacific, Germany has unfortunately "gone mad" again. Accordingly full military and diplomatic preparations must be made for combating a renewed German onset. It is surely not an over-statement to characterize such an account of the contemporary international situation as self-evident nonsense. It cannot really be true that the rulers of Germany suffer from the recurrent attacks of a microbe which impels them to dash themselves, at the utmost risk of their own destruction, upon the rest of the world. Surely there must be some explanation of why it is that to-day, as in 1914, it is the German capitalist group which is driven to threaten the existing system of frontiers, powers, and financial arrangements?

How does the Marxist explanation of why recurrent war is inevitable to capitalism fit in with the realities of this situation? The answer is simple. The German capitalists and landlords were in 1914 and are to-day driven to attempt to change by any means the existing international situation, because their continued existence as capitalists and landlords has become incompatible with that situation. For the present international situation was created at their expense. The British, French, American, and, to a much lesser extent the Italian, capitalists gave themselves (in so far as it was objectively possible) the necessary undeveloped areas, access to the necessary raw materials and markets, and in general the conditions necessary to the maintenance in contemporary conditions of their rates of profit above the minimum level (as defined above). But this could only be done by depriving the German capitalists of precisely those same necessary conditions for their existence.

<sup>1</sup> This is the attitude of the leaders of the British Labour Party, as revealed in their July 1934 pronouncement on the question of the Labour Party's attitude towards war. An "unflinching support" is promised to the British Government in the event of the outbreak of the only kind of war which there is the least likelihood of the British Government desiring to wage.

Sufficient colonies to invest in and to draw raw materials from, and sufficient preserved markets in which commodities might still be sold at a profit, had to be denied to Germany in order to obtain them for the victorious powers.

Nor was this all. The industries belonging to the German capitalists had, and have, an extremely high degree of development. German Westphalia is perhaps the most highly developed area of heavy industry in the world. Its mines, steel works, blast furnaces, by-product plants, power stations, gas works, and engineering shops are (with the corresponding American plants) the most modern and mechanized in the world. But what does this mean in economic terminology? It means that the German capitalists have an extremely high proportion of  $c$  and an extremely low proportion of  $v$  in their total capital. And we know what that means. It means that they can only go on operating their capital profitably, that they can only prevent the very rapid fall in the rate of profit from beginning to diminish their amount of profit, by using to the very utmost all those devices which, we saw, may offset in some measure the falling tendency of the rate of profit. The first of these devices was to screw up the rate of surplus value to the very highest possible degree by keeping wages down to a bare subsistence level, or even, if need be, risking the deterioration of the quality of the labour force by driving wages temporarily below this level. This offsetting factor the German capitalists are now using to the full. But this device carries its own nemesis with it. It destroys all possibility of disposing of anything above a minimum of consumers' commodities at home. Hence the device of screwing up the rate of surplus value must be used in conjunction with other devices, especially that of opening up new external markets, spheres of foreign investment, and sources of raw materials. It is imperative, for example, for the German capitalists not only to make a certain quantum of surplus value on the commodities which they produce, but also to be able to realize this surplus value by selling these commodities. And these commodities can only be sold *abroad* because the very action (the reduction in wages) which made it possible to make an adequate profit on their production, makes it impossible to sell them at home.

Once we have equipped ourselves with Marx's analysis, it



becomes as plain as daylight that the German capitalists must expand or burst. For not only were they deprived, for the benefit of the victor powers, of almost all possibilities of economic expansion: they need these possibilities even more than do the victors. For example, it would have been comparatively easy for the French capitalists to have maintained themselves (though, of course, with diminished wealth) if their empire had been taken and given to the German capitalists instead of the reverse. For the capital of the French capitalists was, and remains, much less highly developed than is the capital of the German capitalists: there is much less *c* and much more *v* in it. Thus from a capitalist point of view the wrong side won the last war.<sup>1</sup> The "best" result of the war, from the point of view of maintaining the capitalist system, would have been for the German capitalists to have acquired a large part of the British and French Empires. Such a result would have brought the territorial partition of the world into a closer correspondence with the actual economic powers of the different contesting capitalist groups.<sup>2</sup> It would have given the capitalists possessing the more developed industries more room for expansion, and those owning the less developed industries less room. But the result was opposite. The younger, more vigorous, yet more highly developed, German group was defeated and was shorn of almost all possibilities of expansion, while the less developed Franco-British group, which already had immense imperial possessions, acquired still more. The result of the war, far from adjusting the political position of the world to the underlying economic reality, produced a still greater contradiction between these two factors.

<sup>1</sup> The eccentricity which is apparent in this conception is due to the fact that in reality there is no such thing as "a capitalist point of view"; there is only a German capitalist point of view, or a British, a French, or an American capitalist point of view. We may, perhaps, be allowed to imagine this non-existent world-wide capitalist point of view (faint hints of which do sometimes appear) for illustrative purposes.

<sup>2</sup> I say, for short, the territorial partition of the world, but, in fact, the question at issue is a wider one than that. The wealth of Britain is maintained not only by the areas actually painted red on the map, but also by semi-developed areas in which Britain's long-established world power has enabled her to acquire a deep stake; the British rate of profit is sustained not only by India, but also by the Argentine. Thus what was in question in the last world war, and will be in question in the next, is something of which colonial expansion is only the most definite and important part. What is in question is world power. For it is the possession of world power which opens up for any capitalist group those opportunities for economic expansion which are in modern conditions indispensable to its existence.

Once this result had been imposed upon the world by the Treaty of Versailles, a return to a war situation in a much shorter time than ever before after a great post-war settlement became inevitable. Lenin elucidated this question in his *Imperialism*, which consists of a masterly application of Marxism to the twentieth-century world situation. A capitalist war, Lenin demonstrated, is, precisely, an attempt forcibly to adjust the balance of political power, as expressed by the territorial division of the world, etc., to the new relative economic preponderances which have grown up since the last war. Germany in 1914 had become the second greatest capitalist state in the world. Her capitalists had on pain of ruin to achieve a corresponding predominance in world power. Instead, almost all their world power was taken from them.

Thus, if this question of the discrepancy between the economic weight and the political world power of the German capitalists was acute in 1914, it is far more acute in 1934. Germany is still economically the second greatest capitalist state in the world. Her vast productive mechanism was more thoroughly and efficiently rationalized during the nineteen-twenties than was any other (with the doubtful exception of the American). The economic preponderance of her capitalists over France and Britain has grown rather than diminished. But, at the same time, the German capitalists have been shorn of almost all access to economic expansion. Is it any wonder that they find themselves in the most desperate situation? Is it any wonder that they know that they must regain all, and more than all, that they have lost in the last war or cease to be capitalists? Do not these circumstances fully account for the desperate and hazardous game which they are now playing? German fascism is the only possible expression of this economic situation. The German capitalists, if they were to survive, had to find some way of clamping down an iron dictatorship at home and of developing offensive strength abroad. Only so was there any chance for them of hewing their way out of the *impasse* in which they found themselves.

How, then, can we characterize the moral strictures which the British, French, and American capitalists see fit to pass upon their German rivals? A hundred fat hands are held up in

horror because the German capitalists are showing that they will stick at nothing, that they will murder and torture without limit, in order to win back their world power and so maintain themselves and their privileges. But will the British, French, or American capitalists do less to prevent the German capitalists from recapturing that world power which they now possess? Truly these latter victorious capitalist groups are not at present so hard pressed as is the German group. They do not yet need to adopt the desperate and hazardous expedients of mass assassination, of pogrom and the like. They reside in a glow of self-righteousness. They thank God that they are not as other men: that their workers are not tortured (but merely half starved), that their public life is still (comparatively) seemly and respectable, and, above all, that they are pacific; that they do not want anybody's territory or privileges, that they do not claim a single thing that they have not already got. *Beati possedentes*—for they shall inherit the kingdom of sanctimoniousness. Holding half the world within their clutch, they look down in shocked disdain at the "mad," "horrible," "criminal" attempts of their dispossessed rivals to challenge their right of possession. What, however, could be more nauseating than this access of moral superiority on the part of the capitalists of the victor states? Of course, the British and French capitalists do not want to have to fight in order to retain their loot. Who does? Of course, they consider it to be criminal of the German capitalists to stake all on a last attempt at empire, rather than throw in their hand without a struggle.

But the workers of Britain, of America, of France, and of Germany will find it hard to decide which is the worse, the desperado, gangster tactics of the ravenous German capitalists, or the uneasy sanctimoniousness of the sated capitalists of the victorious powers.

#### SUMMARY OF CHAPTER XXIII

Incomprehension of the nature of capitalism leads to an acceptance of the fascist claim to be able to solve the crisis, and so to an acceptance of fascism. Mr. Cole's view typical of all

British Labour Party thought. Belief in the possibility of an organized high-wage-paying capitalism in fact common to British Labour leaders, rank and file fascists, brain trusters, American socialists, "progressive" Conservatives, "modern-minded" Liberals, and all "planners." Planned capitalism is the illusory objective of everybody except (a) the revolutionaries, and (b) the responsible capitalist leaders of the system. Great plausibility of this illusion. Difficulty of sufficiently distinguishing the alternative economics, viz., a profit-making economy and a production-for-use economy. Illusion of the possibility of combining the advantages of both with the difficulties of neither. Failure of contemporary popular economists to exhibit this distinction. Guidance, however, indispensable to non-specialists. The tragedy of our lack of an adequate intellectual tradition. Lack of economic theory makes men the blind drudges of the talented adventurers. Economic comprehension the only way of avoiding this humiliating fate. The alternative is the costly school of experience. Predominating importance of economic theory in the epoch of the crisis of a system. Theory as the eye of practice.

How will the economic theory exhibited in this book help us? What the Marxist analysis does, and what it does not, enable us to foresee. Engels' prediction of the last war. The analogous prediction of the present day. Impossibility of understanding the present universal preparations for war unless we understand the nature of the outward drive of every capitalism. Incredibility of non-Marxists' account of the present international situation.

Urgent necessity for the German capitalists, on pain of ceasing to be capitalists, to regain their world power. The acquisition of the conditions necessary to the continued existence of British, French, and American capitalism meant the deprivation of German capitalism of its possibilities of existence. The greater need for access to economic expansion of the more highly developed German capitalism. "The wrong side won the war." Discrepancy between economic weight and political power of the German capitalist group now more marked than in 1914. Hence necessity of fascism at home and war abroad for the German capitalists. Hypocrisy of the "pacifism" of the victorious powers. *Beati possedentes.*

## CHAPTER XXIV

### *The Two Futures*

THE "pacifism" of the sated empires consists in preferring to retain possession of half the world unchallenged, rather than to incur the risks and expenses of beating off a desperate and dispossessed rival. Once the nature and necessities of capitalism have been grasped this is plain enough. But even the wholly disingenuous "pacifism" of the French, British, and American capitalists is more difficult to expose to those who have not this comprehension than is the open gangsterism of the German fascist desperadoes.

Just as the possession and exploitation of vast empires has given the British, French, and to a lesser extent the American, capitalists the economic resources with which they can still buy off their workers with "doles" of one sort or another, so the possession of these empires gives them a power of moral manœuvre also. Not only are they able to pose as the blameless guardians of peace, only too anxious to avoid disturbances of any kind; they are also enabled to prevent a consciousness of the true character of capitalism from dawning upon "their" workers. The leading and classical example of this power of moral and material manœuvre given to a capitalist class by great imperial possessions is to be found in the use made by the British capitalists of their three centuries of Indian exploitation.

Not only have the extra profits derived from the semi-monopolistic exploitation of the three hundred million inhabitants of this sub-continent again and again provided the British capitalists with the wherewithal for softening, by small but timely "doles," the asperities of the class conflict at home.<sup>1</sup> These imperial super-profits have also enabled them to conceal from the British workers the fact that British capitalism also employs all those methods of "lawless" violence, the use of which in Berlin or Vienna is stigmatized as disgraceful. The

<sup>1</sup> The most recent and striking example of this process occurred in the crisis of 1931. It was the sudden and very substantial efflux of gold from the hoardings of India into the vaults of the Bank of England which saved the situation for the British capitalists and enabled them to overcome the acute phase of the crisis while retaining most of the social services. But the situation was saved for them by depleting the last reserve of the Indians.

non-politically conscious members of the British working class have been all too successfully led to suppose that the British capitalists would never dream of doing anything so ungentlemanly as to deprive them of their "traditional liberties"; that the destruction of democratic constitutional forms, the open abolition of freedom of speech, the violent smashing of the workers' organizations, with all the terror and torture which that process involves, are things that could never happen in England. This section of the British workers has had it successfully concealed from them that their relative immunity from capitalist violence has only been obtained by the use of an unrelenting violence in India and in Africa.

The violence which is just as necessary to the existence of British as of German capitalism has in the British case been "externalized." It has been pushed off into Asia and Africa so that a specious sense of peace and harmony may reign within the United Kingdom.<sup>1</sup> Similarly, the existence of that substantial "lower middle class" of functionaries, luxury workers, and personal servants of the better paid type, of the political importance of which we hear a great deal just now, is only possible because of the unseen economic basis of imperial super-profit, derived from semi-monopolistic exploitation.

So long, however, as that basis endures there exists in Britain an unequalled layer of fat, softening and blurring the outlines of the picture of a class-divided society. And just as the fact that the British capitalists already possess those broad imperial possessions for which other capitalist groups have desperately to strive, allows the British capitalists to delude many people about their "pacific intentions"; so the existence, precarious but continuing, of these layers of social fat have prevented in Britain all but the beginnings of any widespread comprehension of class realities. The Marxist analysis of the necessities of capitalism, and the elucidation of the world situation which Marxists base on that analysis, still seem to many English people, who do not care, or have not the opportunity, to look overseas, out of touch with the facts of their everyday life and

<sup>1</sup> The United Kingdom of England, Scotland, Wales and Northern Ireland, that is to say. British imperialism has never been able to hold Southern Ireland without the use of unrelenting violence.

experience. The shallow Liberal-Labour, or "modern minded" Conservative analysis of a functioning capitalist system, in need, no doubt, of substantial reforms, but quite capable of being so reformed, still seems to the great majority of Englishmen to correspond with life as they know it. The possession of an exploitable empire, incomparably larger in proportion to the "Motherland" than has ever existed before in modern history, has quite blinded most British observers to what is happening in the world to-day. It is this which accounts for the appalling "lag" in the consciousness of even the more acute of British political and economic theorists. The social padding made possible by imperial exploitation has enabled British writers and thinkers, and in particular British socialist writers and thinkers, to retain almost without exception beliefs and opinions which were plausible enough in the nineteenth century, but which are catastrophically false to-day. The result is that when the real nature of capitalism in its present stage of development imposes itself, even in Britain; or when they cannot blind themselves any longer to the headlong rush into barbarism of the capitalisms which are unsupported by vast empires, British writers and thinkers are astounded and nonplussed. They can offer not the slightest explanation for what has happened.

The intellectual bankruptcy of these men and women, who in a large measure direct and control the most active minds amongst the British masses, and so, through them, exert a powerful influence upon the masses themselves, is perhaps the most depressing feature of British cultural life to-day. It seems as if British thought, which played so great a part in the nineteenth century enlightenment, cannot advance a step beyond the characteristic conceptions of that epoch. Accordingly, the present epoch becomes increasingly unintelligible to it. British economists like Mr. Cole or Mr. Keynes, writers like Mr. Huxley, poets like Mr. Elliot (if he may now be counted as a British poet), cannot prevent themselves from seeing the ruin of European civilization. But they can only sit by and wring their hands. They either reject, ignore, or misunderstand the only body of thought which can offer a comprehensible analysis of that ruin and its causes. Hence they are totally unable to offer any useful counsel as to how the descent into

barbarism may be arrested where it has fairly begun, or averted elsewhere.

*They are influenced almost exclusively by their day-to-day experience of British life under its present very special, very sheltering, and very temporary, advantages.* Nor must we fail to realize how natural an anti-revolutionary attitude still is on the part of those who have no guiding social or economic theory and who, consequently, are forced to base their views exclusively upon appearances. It is true that even the appearance of British capitalist society to-day betrays many and, it might have been thought, unmistakable signs of decay. We sometimes forget, however, that the progress of that decay is extremely uneven. Lancashire, Durham, South Wales, Glasgow, and the other distressed areas present a startling spectacle of oncoming social degeneration.<sup>1</sup> On the other hand, London, some of the Midland towns and, above all, the parasitic South, still show elements of social progress. Housing conditions, living standards, educational facilities, and the general cultural level of substantial sections of the population in such areas have recently improved, and are in some cases still improving. For those who both turn resolutely away from the black areas, and who are wholly innocent of any body of knowledge which could reveal to them the extreme instability of the basis of the remaining progressive elements to be found in the situation of the prosperous areas, the picture presented by the contemporary British scene is merely inconclusive. They do not see any correspondence between it and the conclusions reached by the Marxist analysis.

Hence they throw their whole influence against any serious study of that analysis. They still tell us that we can expect a new epoch of peace and progress under our present social system. Accordingly they counsel us to preserve and defend that system. They advocate in practice a continuance of precisely those policies which have already in Europe brought on the twilight of human civilization.

In particular the writers, thinkers, and spokesmen of the British Labour Party, who chiefly influence the British masses,

<sup>1</sup> Moreover, British writers and thinkers are never so foolish as to live in, and are seldom so foolish as to visit, Lancashire, Durham, South Wales, or Glasgow.



consistently hold out the illusion of a pleasant, easy, and non-revolutionary issue from the present crisis. We have already analysed the content of this illusion. We have seen that it is based, whether consciously or unconsciously, upon the belief that a new and prolonged period of capitalist stabilization is at hand, a period which will offer the objective possibility of a steady, slow transition to a more socialistic basis of society. This counsel is the deadliest of all the poisons which can be administered to the workers. It is far more dangerous than is any open capitalist propaganda, because, coming from their own leaders and spokesmen, coming from professed and, in many cases, perfectly sincere, socialists, it is believed. Its effect upon the working class is very great. Those possibilities of material and moral manœuvre with which imperial wealth endows the British capitalists in themselves make it hard enough for the British workers to see the true nature of their situation. When their own leaders, also, spend their energies in binding the workers' eyes, their mental liberation becomes a difficult task.

Moreover, by a paradoxical turn, the very difficulty with which the British workers find their way to the truth is used by the more left wing spokesmen of the Labour Party as a reason for not themselves adopting the revolutionary position. We are now often told that it is impossible to tell the revolutionary truth, or to give the example of revolutionary leadership, because it is necessary "to stick to the workers"; to remain, that is to say, a member of the non-revolutionary Labour Party; for the mass of the British workers still belong to that party. Thus the fact that the workers, first drenched with capitalist propaganda, and then subjected to the constant and forceful counter-advice of their own leaders, do not clearly adopt the revolutionary position, is given as the final reason for continuing to prevent them from reaching that position. Because the workers are confused and divided by the fatal counsels of their present leaders, it is impossible, we are now told, to do anything but to continue to confuse and divide them. Because the majority of the organized workers are being deceived into marching down a path which all reason and all experience tells us must lead them to catastrophe, it is impossible, we are informed, to leave that path ourselves or to attempt to persuade

the workers to leave it. On the contrary, we must join their ranks, or rather put ourselves at their head, and lead them straight upon their doom, for to do anything else would be "to cut ourselves off from the workers."

Nor will those who choose this part find it difficult to obtain an influential position. For naturally it is more popular to tell men that they are on the right road, even if we know that they are going to disaster, than to attempt to turn them back. Naturally, it is easier and more acceptable to tell the workers that they have only to mark a ballot paper in the right place every five years in order to end capitalism and produce socialism, rather than it is to tell them that they can only save themselves from death and starvation, and human society from ruin, by a long, fierce, and stubborn struggle. Accordingly, the hold upon the majority of the British workers of those who prefer to prophesy smooth things, whether they still believe them themselves or not, is very great. They are still able to stifle and suppress to a very large degree the struggle of the British workers against fascism and war, the twin children of present day capitalism's necessities.

It is possible that, if Great Britain stood alone in the world, these disastrous leaders would be able to hamper and delay the workers' struggle until it was finally too late. For there is no doubt that if the workers do not at length and in decisive numbers win their way through to a knowledge of revolutionary necessities, then there is nothing which can arrest the decline of civilization by way of fascism at home and war abroad. If the decisive struggle of the workers to free the productive forces from the smothering bonds of capitalist property relations were so hampered and delayed that it became finally unsuccessful, then nothing could prevent the return of barbarism.

And in Britain that struggle has already been long delayed. British capitalism has been in full decay ever since the war. Already whole sections of the British productive apparatus have become permanently unprofitable and are falling into physical ruin. But the appropriate social consequences have been staved off by what is in essence an imperial tribute. And at the same time the very men who should be leading the British workers to the only possible way out of their frightful

situation<sup>1</sup> are using their entire influence to hold them back. No consciousness of the way of escape and consequently no hope of salvation dawns. Despair grows. It seems as if the British working class movement had rotted before ever it was ripe.

"Socialism," that movement used to write upon its banners, "is the hope of the world." The sentence has proved all too true. For as the prospect of the achievement of socialism by the present British Labour movement recedes, the indifference of despair settles upon the British masses. If there did not exist in Britain a small but now increasingly influential revolutionary party, if no outside influence impinged upon Great Britain, if the course of the class struggle in other lands had not been very different and far more decisive, if the absence of any layers of "social fat" was not elsewhere forcing upon the workers a far clearer consciousness of the one way in which they can save both themselves and human civilization, then there would be cause for that despair. It seems probable that British society, taken in isolation, would prove incapable of achieving that decisive break which can alone arrest the present decline of human civilization. If that revolutionary break had not already occurred over a sixth of the world's surface, and if it was not visibly about to occur in much of the rest of it, we could expect nothing but the gradual decay and eventual ruin of human society.

The process would no doubt be neither short nor uninterrupted. The inevitable historical parallel (which, more and more often, is being instinctively drawn by non-Marxist writers) is with the latter centuries of the Roman Empire. That great decline took centuries to run its full course and was several times interrupted by temporary revivals of civilization. In the same way we can well imagine that, if the workers' struggle could be permanently choked and stifled by its present leadership (and that is the one thing that could prevent its success), capitalist civilization as a whole would not be disrupted with the astonishing speed with which the process of barbarization is now proceeding in fascist Central Europe. There would be

<sup>1</sup> In spite of all doles, the situation of the British workers is a frightful one. They are, after all, kindly informed by the Prime Minister himself that "a couple of million" of them will be, even if prosperity returns, "to all intents and purposes in our society superfluous scrap." (J. R. MacDonald, November 22nd, 1932, in the House of Commons.)

a series of wars, and after each war a period of recovery in which the profit-making principle would operate again successfully for a time. Some form of organized society would perhaps hold together for a long time. (Though no stable, if barren, age of the Antonines could be anticipated in the far more dynamic circumstances of the present day.) But it would be a society which had lost hope; a society in which the very best that men could aspire to would be to preserve from further deterioration what measure of civilization they had inherited. It would be a society racked by war and crisis; each period of recovery would be less complete than the preceding one; each catastrophe more destructive of the essentials of civilization.

Fortunately this is only a bad dream born of the stupefaction produced by the inability of even the best contemporary British thinkers to advance an inch beyond either a complacent or a despairing liberalism. Even in Britain there begins to appear a younger generation who are not held in these mental fetters. And in the rest of the world the impact of events is shaking all the most honest and sensitive intelligences into a realization of the true character of man's present predicament.

Let us in conclusion sum up the insight into the present world situation given us by a knowledge of Marxian economics. First, a knowledge of the "economic law of motion" of capitalism enables us to avoid becoming the dupes of the trade cycle. It enables us to avoid prating, with American New Dealers or British Liberal-Labour optimists, of this recovery, unlike all others, being stable and permanent. It allows us to understand why it is that all former recoveries have ended in crises, and why this recovery must also do so.

Next, this knowledge enables us to avoid becoming the dupes of "planning," that illusion which opens the door to fascism. Marx's powerful grasp of the necessities of any system driven by the principle of the accumulation of profit, enables us to understand the real measures which have to be taken to bring capitalist recovery, and to comprehend how strange a name for them is "planning." Marxist economic theory enables us to understand why it is utterly impossible that there can be "a whole new phase of social development," based upon fascist

planned economies. Marxist economic theory, and it alone, enables us to understand what are the real alternatives before us.

We are compelled to face the fact that only two futures are possible for such remaining capitalist democracies as France, Britain, and America. Either the rate of profit must once again be restored, by any methods and at any price in human suffering and social degradation, or revolutionary working-class movements must expropriate the capitalists and organize profitless production for use. It is the purpose of fascism to effect the first alternative, as it is the purpose of communism to effect the second. Moreover, some form of fascism with all its nauseating consequences, is to-day just as essential for a more than momentary restoration of the rate of profit as is communism for the victory of the workers and the organization of production for use. It is quite impossible for the ruling capitalists to put through the preposterous wage cuts and general worsening of conditions which, as we have seen in precise detail, are now necessary for any but the briefest and most partial restoration of the rate of profit, without smashing all working-class organizations capable of offering resistance. This, and no idle nonsense about planning, is the function of fascism. This, the pulverization of everything that stands in the way of renewed profit-making, is fascism's be-all and end-all. Nor have we denied that for a time fascism may succeed in restoring the rate of profit. The fascist leaders and backers do not share any of the illusions about "planning" which they have so carefully instilled into their supporters. They go straight for what is undoubtedly the only possible capitalist policy. But we have also seen that the restoration of adequate profitability to industry by gigantic wage cuts, although the only thing that the capitalists can do, also carries with it its own nemesis of renewed crisis. Capitalism, no less when guided by fascist hands than before, is ultimately bound to pierce itself on one or other of the horns of its dilemma. At the very most the fascists can give the system a brief period of hectic and unstable revival, before they plunge with it into the next crisis and the next war.

And after that? After that, wherever capitalism is still in existence, the shadows darken. After that, there can only follow for the capitalist areas of the world an ever more rapid decay. We shall see in those areas the permanent contraction of

production, the permanent abandonment of all those productive forces, animate and inanimate, which it has become permanently unprofitable to use. Fascism will reveal itself ever more clearly (if better evidence is needed than the Germany of 1934) as "the organization of social decay," as R. P. Dutt calls it. The essential use, then, of Marx's economic discoveries is to enable us to see the alternatives which face us. And these alternatives are, as he himself expressed it—barbarism or communism.

But Marx's discovery does not in itself give us any assurance that capitalism will be followed by communism. There is no guarantee of an automatic ascent to Utopia contained in that law of motion of the capitalist system which Marx revealed. Marx's discovery, like any other scientific discovery, must be used in order to become significant. What it gives us is the knowledge which alone makes it possible for us to control our destiny. But it does not, and cannot, guarantee that we shall make use of that knowledge. Marx's discovery might lie unused and be for a time forgotten as has many another of the conquests of the mind of man. Powerful forces are always attempting to make us ignore or forget it. The whole formidable apparatus of the ruling class is perpetually engaged in the attempt first to ignore, when that becomes impossible to distort, and then finally to suppress absolutely, the discoveries of Marx. Were it possible for them to succeed, they would not be able to save capitalism, or even much to prolong its existence. But what they *could* achieve would be to ensure that capitalism was followed, not by a new and higher order of civilization based on men's conscious organization of their work in a society freed from the existence of warring social classes, but by a new age of barbarism.<sup>1</sup>

This was the alternative which Marx steadily presented. It was certain, he knew, that capitalism, like every previous social system, would come to the end of its possibilities of existence.

<sup>1</sup>A modern poet has felt and expressed the vile possibility of a progressive breakdown of civilization.

"... like history in Dark Ages where  
Truth lies in dungeons from which drifts no whisper :  
We hear of towers long broken off from sight  
And tortures and war in dark and smoky rumour,  
But on men's buried lives there falls no light."

(Stephen Spender. Poems.)

Then mankind would have to find its successor. But that successor might be either communism or barbarism. And the choice depended upon the extent to which men achieved, and then acted upon, an understanding of reality sufficiently comprehensive to enable them to carry civilization, unbroken, from one basis to another. Men, he taught, can make their own history, "but not just as they please." The sum of things imposed circumambient conditions upon them. In our epoch they impose this choice between communism and barbarism. Moreover, men will only be able to choose the indefinitely wide opportunities offered by communism, and avoid the almost unimaginable frustrations involved in a decline to barbarism, if they learn *how* to make their history.

For the science of making history, which is another name for politics, depends for its success, like every other science, upon a knowledge of the limiting conditions. The chemist succeeds where the alchemist failed because he knows what he cannot do : he knows what is inherently impossible. Hence he can concentrate upon exploring experimentally the finite field of the possible. He knows the determinate relationships, or rather some of them, of his field of action. Similarly, by political action men may succeed in substituting a new basis for civilization before the old has utterly broken down ; but only if their action is guided by an adequate knowledge of what is inherently impossible, of what it is a vain dissipation of our finite resources of creative energy to attempt.

We see being fought out before our eyes the world-wide and desperate struggle which will decide whether the world passes to communism or to barbarism. I do not think that the issue of that struggle is in doubt. The existence for the first time in history of two factors, namely, a very great community already upon the road to communism and of a world-wide, unified, and disciplined, if as yet insufficiently large, revolutionary organization, is a decisive guarantee that our century will be the century of the transition to communism, and not of the transition to barbarism. It is unthinkable that the disruption of capitalist civilization, as it spreads from Central Europe over the rest of the world, will not give a dozen opportunities for successful workers' revolution, and give them before the necessary material and

cultural bases of communism have been wholly destroyed. But how far down the dreadful path to the dark ages the world must go, how much of the achievements of capitalist civilization must be lost, how much blood and agony and horror must be piled up, greatly depends upon the rapidity with which men achieve a conscious comprehension of the determinate social and economic relationships of to-day.

If, in particular, those men and women who are in a position to influence the working-class movements in the remaining capitalist democracies refuse to learn anything from experience or from reason, if they blindly cling to their illusory belief in the possibility of a reformed, planned, high-wage-paying capitalism, quietly but quickly transforming itself into socialism; if they use their influence and power to fasten this illusion upon the workers, then, no doubt, the transition to communism will only be achieved at an appalling cost. For the one substitute for adequate social and economic theory is the rediscovery of reality by the method of trial and error. The working-class movements will in this case have to go through the purgatory of learning from the brutal lesson of events both what is the true nature of capitalism, and what is the only way of their salvation.

This frightful process can be enormously shortened, and even in a great measure avoided, by the use of that body of social and economic science which Marx bequeathed to us. Equipped with this knowledge, men will comprehend the necessity of revolution. In decisive numbers they will take their places in that revolutionary army whose unseen battalions are forming in every country of the world, and upon whose success rests the hope and future of mankind.

#### SUMMARY OF CHAPTER XXIV

Power of material and moral manœuvre given to the capitalists of the victorious empires by imperial super-profits. Violence used by the British capitalists "externalized" on to India and Africa. Specious sense of peace and security within Britain. Consequent inability of British writers and thinkers to comprehend the essential nature of contemporary capitalism. Their



inability to advance at all beyond characteristic nineteenth-century conceptions. Their considerable influence used to fasten the illusion of a coming period of capitalist stabilization upon the British workers. The influence of the theorists of the Labour Party used to blind the workers to their real situation. The difficulty with which the British workers arrive at a comprehension of the revolutionary truth given as an excuse for further deceiving them. Formidable hold over the workers' minds of those who prefer to prophesy smooth things.

Possibility that the British workers, if taken in isolation, would not achieve an adequate revolutionary consciousness. The Labour Party rotten before it was ripe. The inevitable decline of civilization can only be interrupted by revolution.

Summary of what a knowledge of Marxist economic theory can do for us. (i.) It enables us to avoid becoming the dupes of the trade cycle. (ii.) It enables us to avoid becoming the dupes of planning. (iii.) It enables us to see what are the only alternatives before us, namely, communism or barbarism.

The fascist road to barbarism. Necessity of using Marx's discovery. It shows us *how* we can save ourselves. But, in itself, it gives us no guarantee of salvation. The capitalist attempt to suppress Marx's discovery would not if it succeeded save capitalism ; but it would ensure that the world passed to barbarism, not to communism.

The issue of the struggle between the forces making for communism and the forces making for barbarism not in doubt. The existence of the U.S.S.R. and of a world-wide, disciplined and organized, although as yet insufficiently strong, revolutionary movement are assurances that some of the many opportunities for revolt which will be given by the chaotic decay and internecine wars of capitalism, will be taken. The supreme value of Marx's discoveries are that their use can enormously shorten the agonies of the period of capitalist decay, and hasten the establishment of the new basis of civilization.



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